DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

A Message from the Secretary of the Treasury

The 2008 Financial Report of the United States Government, issued by the U.S. Department of the Treasury, is a comprehensive financial report that provides a backdrop for both the Government's current financial position and prospects for moving forward.

The Government's net operating cost for the fiscal year that ended September 30, 2008 was just over $1 trillion, more than triple the net operating cost for the prior fiscal year. The growth in the net operating cost resulted from the economic slowdown, the Government's response to the slowdown and significant re-estimates of the Government's liabilities for veterans' disability compensation benefits. Government revenues stayed relatively flat, increasing only 1 percent, while net costs increased by 25 percent from fiscal year 2007 to fiscal year 2008. The cost increases resulted primarily from agencies' substantial re-estimates of liabilities for post-employment benefits. The Government's budget deficit for the fiscal year that ended September 30, 2008, was $455 billion, which was more than double the deficit for the prior year.

The report discusses the Government's long-term fiscal challenge of funding the Social Security, Medicare and Medicaid programs. In both the near term and long term, these programs will account for a large and growing portion of total Government spending. The projected long-term costs are much greater than the resources that will be available to pay for them, particularly as health care costs continue to rise and the population continues to age. Changes are needed to bring these important programs into fiscal balance.

The report also discusses the steps the Federal Government has taken to restore stability in the U.S. financial system. The Treasury Department continues to work to achieve and maintain the stability of the financial system given our authority and capacity. I am confident that with all parties working cooperatively in this unprecedented situation, we will find solutions that restore and maintain our national economic well-being.

Henry M. Paulson, Jr.

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MANAGEMENT'S DISCUSSION AND ANALYSIS

Introduction

The fiscal year (FY) *2008 Financial Report of the United States Government (Report)* provides the President, Congress, and the American people a comprehensive view of the Federal Government's finances, i.e., its financial position and condition, its revenues and costs, assets and liabilities, and other obligations and commitments. The Report also discusses important financial issues and significant conditions that may affect future operations. This year's Report gives particular emphasis to two key issues: The Government's response in recent months to the financial market crisis, and the Government's capacity to sustain the funding and pay the benefits of key social insurance programs, such as Social Security and Medicare.

Pursuant to 31 U.S.C. § 331(e)(1), the Department of the Treasury must submit the Report, which is subject to audit by the Government Accountability Office (GAO), to the President and Congress no later than six months after the September 30 fiscal year-end. To encourage timely and relevant reporting, the Office of Management and Budget (OMB) accelerated both agency and governmentwide reporting deadlines to 45 days and 75 days after year-end, respectively.

FY 2008 Agency Audit Results				
Unqualified				Disclaimer
USDA	HUD	DoT	NSF	
Commerce	Interior	VA	NRC	Defense
Education	Justice	USAID	OPM	DHS [1]
Energy	Labor	EPA	SBA	State
HHS	Treasury	GSA	SSA	NASA

[1] Balance Sheet and Custodial Statement Audit Only

The Report is prepared from the audited financial statements of specifically designated Federal agencies, including the Cabinet Departments and many smaller, independent agencies (see organizational chart on the next page). For FY 2008, GAO has issued a 'disclaimer' of opinion on the accrual-based consolidated financial statements, as it has for the past eleven years, for the fiscal years (FY) ended September 30, 2008 and 2007. This means that sufficient information was not available for the auditors to determine whether the financial results were reliable. In FY 2008, 20 of 24 of the most significant agencies earned unqualified opinions on the financial statement audits. In addition, the Government earned an unqualified audit opinion on a Report component - the Statement of Social Insurance (SOSI) - for the second year in a row, indicating the auditor's opinion that the SOSI fairly presents the financial condition of the programs covered in that statement.

The FY 2008 *Financial Report* consists of:

- Management's Discussion and Analysis (MD&A), which provides management's perspectives on and analysis of information presented in the Report, such as financial and performance trends;
- The principal financial statements and the related footnotes to the financial statements;
- Supplemental and Stewardship Information; and
- GAO's Audit Report.

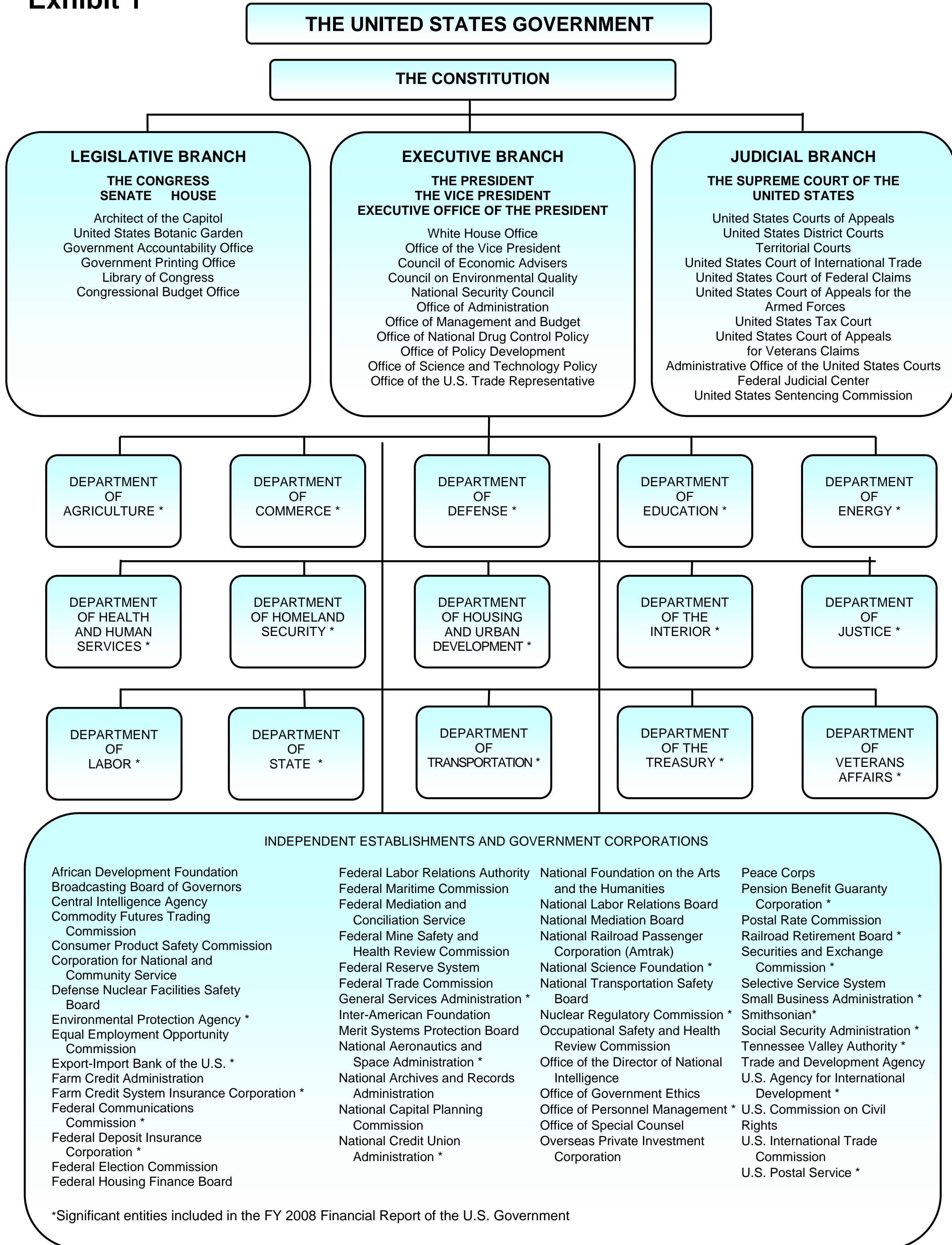
In addition, for the second consecutive year, the Government has produced a Citizens' Guide to provide the American taxpayer with a quick reference to the key issues in the Report and an overview of the Government's financial health.

Mission & Organization

The Government's fundamental mission is derived from the Constitution: ***"…to form a more perfect union, establish justice, insure domestic tranquility, provide for the common defense, promote the general welfare and secure the blessings of liberty to ourselves and our posterity."*** The Congress authorizes and agencies implement programs as missions and initiatives evolve over time in pursuit of key public services and objectives, such as providing for national defense, promoting health care, fostering income security, boosting agricultural productivity, providing veteran benefits and services, facilitating commerce, supporting housing and the transportation systems, protecting the environment, contributing to the security of energy resources, and helping States provide education.

Exhibit 1 on the following page provides an overview of how the U.S. Government is organized.

Exhibit 1



The Government's Financial Condition

A complete assessment of the Government's financial or fiscal condition requires analysis of historical results, projections of future revenues and expenditures, and an assessment of the Government's long-term fiscal sustainability. As discussed later in this Report, the Government's financial statements show its financial position at the end of the fiscal year, explain how and why the financial position changed during the year, and provide insight into how the Government's financial condition may change in the future. In particular, the Statement of Social Insurance (SOSI) compares the actuarial present value of the Government's anticipated expenditures for future scheduled benefits to its expected collections (e.g., taxes and premiums) for Social Security, Medicare, and other social insurance programs over a 75-year period. Expected expenditures for other major programs, including defense, Medicaid and education, and future tax revenues, while not presented in the SOSI, will also affect the Government's future fiscal condition, as will the Government's recent efforts to stabilize the economy.

What Does This Mean to Me?
2008 marked a departure from the recent pattern of declining deficits. Market stabilization efforts are expected to contribute to potentially substantial deficit increases in the coming year.

The natural starting point for assessing the Government's long-term financial condition is its current financial position, both in absolute terms and in relation to the economy as a whole. Gross Domestic Product (GDP) measures the size of the Nation's economy in terms of the total value of all final goods and services that are produced in a year. It serves as a useful indicator of the economy's capacity to sustain the Government's many programs. For example, in FY 2008:

- Government cash-based outlays of $3.0 trillion, net of receipts of $2.5 trillion (approximately 21 percent and 18 percent of GDP, respectively) yielded a record unified budget deficit for FY 2008 of $454.8 billion. Similarly, the Government's net operating cost more than tripled – from $275.5 billion in FY 2007 to just over $1 trillion in FY 2008.
- The Government borrows from the public to finance the gap between cash-based outlays and receipts (commonly referred to as the unified 'budget deficit'). The value, including interest, of publicly held debt was 40.8 percent of GDP at the end of FY 2008.
- The social insurance programs and Medicaid have become a large share of Government cash-based expenditures. Forty years ago, Medicare, Medicaid, and Social Security accounted for 16 percent of total Government expenditures. Today, they comprise 40 percent of all expenditures.

The following pages contain a more detailed discussion of the budget, the economy, and the debt, as well as a long-term view of the Government's ability to meet its obligations for social insurance and market stabilization.

Budget Deficit vs. Net Cost

Each year, the Administration issues two reports which detail the financial results for the Government. The ***President's Budget*** (Budget), the Government's primary financial planning and control tool, describes how the Government spent and plans to spend the money it collects. By comparison, the accrual-based ***Financial Report of the United States Government*** (Report) includes the cost of operations, the sources used to finance those costs, how much the Government owns and owes, and the outlook for its social insurance programs.

Table 1: Budget Deficit vs. Net Operating Cost

Dollars in billions	2008	2007
Budget Deficit	**$454.8**	**$162.8**
Change in:		
Federal Employee and Veteran Benefits Payable	$549.8	$90.1
Environmental & Disposal Liabilities	$0.8	$36.8
Capitalized Fixed Assets, Net	($46.6)	($2.6)
Other	$50.3	($11.6)
Net Operating Cost	**$1,009.1**	**$275.5**

In FY 2008, the Government incurred a record high unified budget deficit of $454.8 billion, more than doubling the FY 2007 deficit of $162.8 billion. This historic increase was due in great part to the combined effect of the developing weakness in the economy and the Government's response to that weakness. Because of the weakening economy, corporate tax revenues declined by $68 billion. These factors also contributed to the increase

in the Government's net operating cost, which jumped to just over $1 trillion – more than three times the 2007 net operating cost of $275.5 billion. Net operating cost also increased due to agencies' substantial reestimates of liabilities for postemployment benefits. The Departments of Defense, Health and Human Services, and Veterans' Affairs, and the Social Security Administration, as well as interest on the Federal debt accounted for the majority of the Government's net costs. Table 1 shows that $549.8 billion changes in estimates of the Government's net postemployment liabilities to its military and civil service employees accounts for most of the difference between the Government's unified budget deficit and net operating cost. This issue is discussed further in the 'Where We Are' section of this document.

The Economy in Fiscal Year 2008

A review of the Nation's key economic indicators can add context to a discussion of the Government's financial results. As summarized in Table 2, the U.S. economy slowed noticeably in FY 2008, and it fell into recession in December 2007, three months into the fiscal year. Growth was significantly restrained for the third straight year by the ongoing slump in the residential homebuilding sector. In addition, consumer spending grew modestly during the first three quarters of the fiscal year, and then showed its sharpest one-quarter decline since 1980 in the final quarter. Record high energy prices through most of the year and elevated food prices dampened consumer confidence. Mounting financial market losses also weighed on confidence. The turmoil in the financial sector limited credit availability, further contributing to sagging consumption.

Table 2: Economic Indicators

National Economic Indicators	FY 2008	FY 2007
Real GDP growth	0.7%	2.8%
Residential construction growth	-20.9%	-17.0%
Average monthly payroll job increase (thousands)	-43	109
Unemployment rate (percent, end of period)	6.1%	4.7%
Consumer price index (CPI)	5.3%	2.4%
CPI, excluding food and energy	2.5%	2.1%
Treasury constant-maturity 10-year rate, (end of period)	3.9%	4.6%
Moody's Baa bond rate (end of period)	7.8%	6.6%

Employment fell beginning in January 2008, and the unemployment rate rose. Inflation was dominated by significant increases in energy and food prices, but underlying inflation remained relatively stable. Partly as a result of higher overall inflation, real wages fell throughout FY 2008 on a year over year basis. Corporate profits, outside the energy sector, weakened or declined. Federal tax receipts remained relatively constant and spending growth accelerated in FY 2008. As a result, the Federal unified budget deficit rose to $454.8 billion, or about 3.2 percent of GDP (compared to 1.2 percent in FY 2007).

After rising at an annual average rate of 2.8 percent during FY 2007, real GDP growth slowed to 0.7 percent over the four quarters of FY 2008. Quarterly performance was quite volatile. Growth was noticeably stronger in the third quarter of the fiscal year (2.8 percent), boosted in large part by a narrowing trade deficit and the spring stimulus payments, but real GDP declined 0.5 percent in the final quarter of the fiscal year. Residential fixed investment declined at double-digit rates in each of the fiscal year's four quarters, reflecting another year of sharply weaker housing demand. Nonresidential fixed investment growth slowed markedly during the fiscal year.

The following key points summarize economic performance in FY 2008.

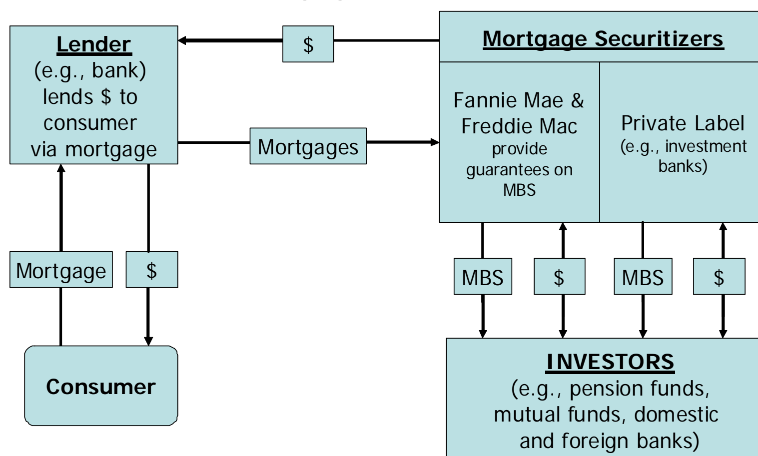
- After increasing by 2.7 percent in FY 2007, consumer spending was slightly negative over the four quarters of FY 2008, with a notable slowing in the final quarter.
- Exports have been a key driver of the economy, maintaining a steady pace of growth in FY 2008 and accelerating markedly during the latter half of the fiscal year, but the outlook for exports is uncertain in view of the spreading world-wide recession.
- Labor market conditions deteriorated during FY 2008. Nonfarm payroll employment declined at an average rate of 68,000 jobs per month in FY 2008, compared with the 109,000 average increase in jobs per month in FY 2007. From the employment trough of August 2003 through December 2007, the economy created 8.3 million new jobs, but between December and the end of FY 2008, employment fell by about 1 million.

- The unemployment rate trended steadily higher throughout FY 2008, reaching 6.1 percent at the very end of the fiscal year, compared to 4.7 percent at the end of FY 2007.
- Overall inflation, as measured by the consumer price index (CPI), advanced to 5.3 percent in FY 2008, up significantly from the 2.4 percent pace of FY 2007. Core inflation (which excludes food and energy) remained relatively contained, however, rising to 2.5 percent in FY 2008 versus 2.1 percent in FY 2007.
- Financial market turbulence intensified during the last few months of FY 2008, as uncertainties about the value of mortgage-market-related assets led investors to reappraise asset values in a variety of markets. This turbulence reduced credit availability. For example:
    - Corporate debt yields reached about 450 basis points above Treasury securities in late September 2008, compared with about 175 basis points in August 2007;
    - The difference between the 3-month London Interbank Offered Rate (LIBOR)[1] and the risk-free 3-month Treasury rate shot up to nearly 550 basis points in late September 2008 (after averaging less than 50 basis points in 2006 and much of 2007).

Market Stabilization Efforts

Volatility in the mortgage and credit markets during the last half of FY 2008 sparked unprecedented economic events. Efforts to restore financial stability began in earnest in March with the Federal Reserve's[2] support of JP Morgan Chase & Co. in its acquisition of The Bear Stearns Companies, Inc. (Bear Stearns). Bear Stearns had been considered one of the leading U.S. investment firms, with much of its investment portfolio tied to sub-prime mortgage-backed securities (MBS). Declines in the sub-prime credit market precipitated significant portfolio losses and a substantial cash shortfall not only at Bear Stearns, but eventually across many other major financial and credit institutions who had invested heavily in MBS in recent years. The MBS market played a key role in the deterioration of credit market conditions in FY 2008. Exhibit 2 provides an illustration of how individual mortgage loans are transformed into MBS.

Exhibit 2: Mortgage Securitization Process



MBS performance was directly dependent on the performance of the underlying mortgages and loans that comprised the security. A developing recession, housing market declines, including falling property values and demand, a decline in the value of the U.S. dollar, significantly increased availability and use of sub-prime loans (with limited homeowner equity), and increased mortgage defaults and foreclosures placed tremendous pressure on the MBS market, particularly the sub-prime portion of the market. Mounting losses compelled MBS investors, in particular bank investors, to retain whatever funds they could and minimize their exposure by being reluctant and, in some cases, refusing to make loans. This would ultimately lead to a 'frozen' credit market. Due to the inherent relationship between the MBS and the underlying loans, this freeze impacted a wide array of investors – from the prospective homebuyer seeking a mortgage on a first home, to the multimillion dollar corporation seeking short-term financing so that it could meet payroll. In addition, failing mortgage loans precipitated a surge in foreclosures.

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[1] LIBOR is the interest rate at which banks can borrow funds from other banks in the London interbank market. Set daily by the British Bankers' Association, it is the most widely used benchmark for short term interest rates.

[2] The Federal Reserve is the central banking system of the United States. It is a quasi-public (government entity with private components) banking system composed of (1) the presidentially appointed Board of Governors of the Federal Reserve System in Washington, D.C.; (2) the Federal Open Market Committee; (3) twelve regional Federal Reserve Banks located in major cities throughout the nation acting as fiscal agents for the U.S. Treasury; (4) numerous private U.S. member banks; and (5) various advisory councils. Since February 1, 2006, Ben Bernanke has served as the Chairman of the Board of Governors of the Federal Reserve System.

This precarious environment eventually led to the demise of such long-established firms as Lehman Brothers, and to transformations within or acquisitions of other major institutions, such as Wachovia Bank, Washington Mutual Bank, and American International Group (AIG). It also placed the financial future of both the Federal National Mortgage Association (Fannie Mae or Fannie) and the Federal Home Loan Mortgage Corporation (Freddie Mac or Freddie) in jeopardy. Something had to be done to restore investor and lender confidence and to get the credit pipeline flowing again. In response, the Treasury Department championed two legislative efforts in attempts to restore consumer confidence and market stability.

The Path to Recovery, Part I – HERA

In July 2008, Congress passed the Housing and Economic Recovery Act (HERA) of 2008, based on concern that continued losses at Fannie and Freddie and throughout the U.S. housing/credit market could lead to significantly larger and broader problems for both the U.S. and foreign economies. HERA established a new regulatory agency: the Federal Housing Finance Agency (FHFA) with enhanced regulatory authority over the housing Government Sponsored Enterprises (GSEs)[3], including the capital requirements and business activities of Fannie Mae and Freddie Mac. HERA also provided the Treasury Secretary with temporary authority to purchase any obligations and other securities issued by the housing GSEs.

Due to deteriorating conditions in the housing mortgage markets and the resulting negative financial impact on Fannie Mae and Freddie Mac, FHFA placed them under conservatorship on September 7, 2008. This action was taken to preserve GSE assets, ensure a sound and solvent financial condition, and mitigate systemic risks that contributed to current market instability. Placing Fannie Mae and Freddie Mac under protection of a conservatorship enabled the Government to avert the initial threat of failure and focus on the larger, systemic challenges, with the ultimate intention of restoring financial stability. Under the conservatorship, the conservator (FHFA) replaced the organization's senior management and oversaw the continued operation of the GSEs. Pursuant to the authorities provided to the Secretary of the Treasury under the HERA, the Treasury Department, on September 7, 2008, took three additional steps to help ensure the solvency and liquidity of the GSE while they are working to resolve their financial difficulties:

- entering into senior preferred stock purchase arrangements with Fannie Mae and Freddie Mac;
- establishing a GSE credit facility; and
- establishing a GSE MBS purchase program.

HERA established the HOPE for Homeowners Program[4], which provides another stop-gap measure by helping borrowers faced with foreclosure refinance through the Federal Housing Administration. Despite these actions, there was still a pressing need to address the more systemic challenges posed by the credit crisis.

The Path to Recovery, Part II – EESA and TARP

In October 2008, Congress passed and the President signed the Emergency Economic Stabilization Act (EESA), which authorized Treasury to establish and manage the Troubled Asset Relief Program (TARP). In general, TARP authorizes the Government to provide additional protection and stability to financial markets through a wide array of mechanisms:

- EESA authorizes the Government to purchase or insure up to $700 billion in troubled assets, such as securities and other financial instruments.
- The Treasury Secretary had immediate access to the first $250 billion. Following that, an additional $100 billion was authorized by the President. The last $350 billion is subject to Presidential approval and Congressional review. In its first use of the TARP, Treasury created the Capital Purchase Program (CPP) to purchase up to $250 billion in senior preferred shares in a wide variety of banks and other financial institutions. These will be largely non-voting shares, may be sold to a third party, and will pay a 5 percent dividend in the first 5 years, and 9 percent thereafter.

[3] The housing GSEs (Fannie Mae, Freddie Mac, and the Federal Home Loan Bank System) are chartered by the Federal Government and pursue a federally mandated mission to support housing finance. Some GSEs are distinctly established as corporate entities - owned by shareholders of stock traded on the New York Stock Exchange. The operations of the housing GSEs are not guaranteed by the Federal Government.

[4] HOPE for Homeowners is a voluntary program for the refinancing of distressed loans by providing Federal Housing Administration (FHA) insurance for refinanced loans that meet certain eligibility requirements. Both borrower and lender must agree to participate in the program.

- Any firm participating in the CPP will provide the Treasury Secretary with a warrant guaranteeing the right to purchase additional common shares worth up to 15 percent of the value of the preferred stock purchased. The purchase price will be the average stock selling price over the 20-day period before the preferred stock purchase. If the company is unable to issue a warrant, it may issue senior debt instead.
- EESA provides for: (1) oversight by the Government Accountability Office (GAO) and a Special Inspector General; and (2) transparency by requiring Treasury to make available an electronic description of assets acquired under the program.

Recovery Efforts and Actions

The following summarizes some of the recovery efforts to date and their impact on and implications for the Government's consolidated financial statements. It should be noted that, although HERA and EESA authorize the Government to spend hundreds of billions of dollars in the recovery effort, the majority of those funds have yet to actually be spent, and as a result, are not and would not be reported on the Government's consolidated financial statements. Generally, the Government has recorded the funds that have already been spent at cost. The Government expects to recover, if not earn a return on these funds.

Actions by Congress:

- Passes HERA, which enhanced the regulatory framework and provided temporary authority for the Treasury Secretary to provide financial support to Government Sponsored Enterprises (GSEs).
- Passes EESA, establishing the Troubled Asset Relief Program (TARP), authorizing the Treasury Department to use up to $700 billion in support of market stabilization efforts. The $700 billion limit shall be reduced by the difference between outstanding and guaranteed obligations under the EESA-authorized insurance program, if any, and the balance in the Troubled Assets Insurance Financing Fund (TAIFF), established by EESA to guarantee timely payments on mortgage-related assets.
- Legislation only authorizes the Government to engage in specified market relief efforts. Authorizations by themselves do not impact either the Government's financial statements or the deficit - the exercise of those authorities do.

Actions by the Federal Reserve System (Fed)

- Lends approximately $30 billion in support of JP Morgan Chase to facilitate its acquisition of Bear Stearns;
- Agrees to lend up to $85 billion to American International Group (AIG). Subsequent to FY-end 2008, the credit facility was modified and Treasury agreed to purchase $40 billion in Senior AIG preferred stock and will receive common stock warrants for 2 percent of the outstanding AIG common stock;
- Announces Money Market Investor Funding Facility through which the Fed is authorized to buy $600 billion in CDs and commercial paper to bolster money market mutual funds, and sets up separate facilities to purchase certain AIG assets;
- Agrees to guarantee $306 billion of Citigroup troubled assets. Pursuant to the agreement, Citigroup would cover the first $37 billion in losses, Treasury would cover the next $5 billion, and FDIC would cover up to $10 billion of additional losses. Treasury and FDIC receive Citigroup preferred stock as part of the arrangement;
- Announces program to purchase up to $500 billion of mortgage-backed securities and up to $100 billion of Fannie and Freddie debt, and to lend up to $200 billion against new car, student, and small-business loans. Treasury has pledged $20 billion from TARP for this program as well;
- Under the Supplementary Financing Program, Treasury borrowed $300 billion to increase cash balances at the Fed to support the Fed's market stabilization efforts.

The vast majority of Fed actions and transactions will not directly impact the Government's financial statements since the Fed is an independent entity and, while part of the Government, is not considered part of the Federal Government reporting entity. To date, the Government's exposure is largely limited to any impact that losses from these programs may have on excess profits that the Fed is required to pass on to the Treasury's General fund.

Actions by Treasury:

- Under HERA authority, received preferred stock and warrants, valued at $7 billion as consideration for entering into assistance agreements - recorded as an investment. Commits to provide up to $200 billion under a preferred stock purchase agreement to ensure that GSEs' assets and liabilities remain in balance – records $13.8 billion as a liability in FY 2008, based upon the Federal Housing Finance Agency's notification to the Treasury Department that a payment is due to Freddie

Mac, based on Freddie Mac's September 30, 2008 net worth status. Fannie Mae did not require a payment in FY 2008. Purchased $3.3 billion in MBS and recorded that amount as a loan receivable in FY 2008.

- Under EESA, used over $200 billion to purchase assets of qualifying financial institutions since fiscal year-end as of December 9, 2008. None of these purchases occurred during FY 2008.

Amounts expended under HERA and EESA have been and are expected to be treated as either investments or loans, as the Government may recover and possibly even earn a positive return on amounts invested as economic conditions improve.

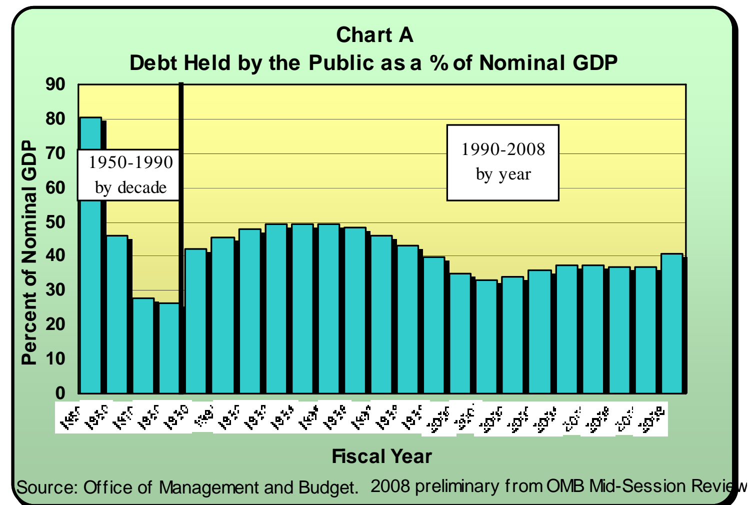
As the first quarter of FY 2009 draws to a close, the Government is exploring a number of other recovery strategies. Actions under HERA, EESA, and other initiatives are intended to restore confidence to lenders and consumers, and provide stability to the nation's economy.

Federal Debt

As noted earlier, the unified budget surplus or deficit is the difference between total Federal spending and receipts (e.g., taxes) in a given year. The Government borrows from the public (increases Federal debt levels) to finance deficits. During a budget surplus (receipts exceed spending), the Government typically uses those excess funds to reduce the debt borrowed from the public. Historically, the Government has incurred debt when: (1) it borrows from the public to fund budget deficits, and (2) government funds invest excess receipts in government securities. However, in FY 2008, this relationship changed, with Treasury borrowing over $300 billion to increase cash balances at the Fed so that the Fed can assist with market stabilization efforts. The implementation of both HERA and EESA including the Troubled Asset Relief Program (TARP) have the potential to increase future borrowings by more than $1 trillion. Substantial borrowings in FY 2009 and beyond are expected to fund stock and asset purchases at financial institutions across the country.

At the end of FY 2008, the Government had incurred $10 trillion in debt, comprised of: debt held by (or owed to) the public (i.e., publicly held debt) and intragovernmental debt (i.e., debt the Government owes to itself). Publicly held debt (a balance sheet liability) includes all Treasury securities (e.g., bills, notes, and bonds) held by individuals, corporations, Federal Reserve banks, foreign governments, and other entities outside the Government. Intra-governmental debt is primarily held in the form of special nonmarketable securities by various parts of the Government. Laws establishing Government trust funds generally require excess trust fund receipts to be invested in these special securities. Intra-governmental debt is not shown on the balance sheet because claims of one part of the Government against another are eliminated for consolidation purposes (see Financial Statement Note 11).

Gross Federal debt (with some adjustments) is subject to a statutory ceiling (i.e., the debt limit). Prior to 1917, the Congress approved each debt issuance. In 1917, to facilitate planning in World War I, Congress established a dollar ceiling for Federal borrowing, which has been periodically increased over the years (most recently from $9.8 trillion to $10.6 trillion in 2008). At the end of FY 2008, the amount of debt subject to the limit was $9.96 trillion, $655.2 billion under the limit. In October 2008, in connection with the passage of EESA, the limit was raised again to $11.3 trillion.



Publicly Held Debt as a Percentage of GDP

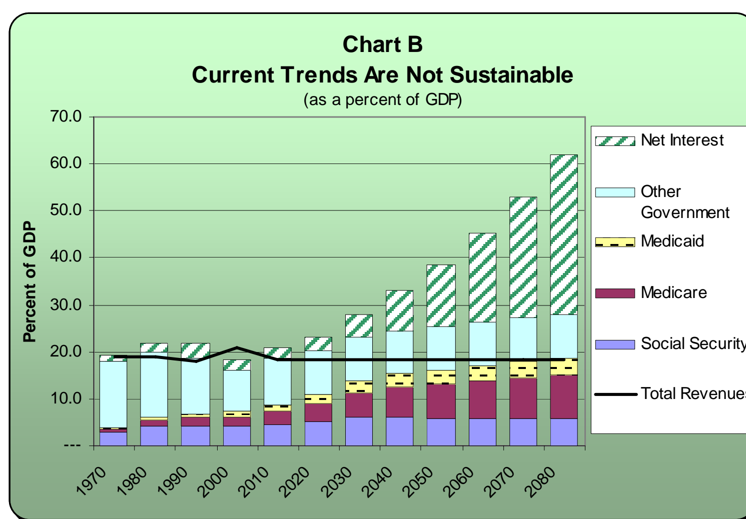
The Federal debt held by the public as a share of GDP (Chart A – on the previous page) compares a country's debt level to the size of its economy over time. In the late 1970s, increasing budget deficits spurred an increase in publicly held debt, which essentially doubled as a share of GDP over a 15-year period, reaching about 50 percent in

1993. The budget controls instituted by the Congress and the President, together with economic growth, contributed to declining deficits and emerging surpluses at the end of the 1990s. This improved fiscal performance led to a decline in publicly held debt, (from 43 percent of GDP to about 33 percent from 1998 through 2001). In fiscal years 2002 through 2004, the debt-to-GDP ratio started to rise slightly, due to many factors, including increased spending for homeland security and defense commitments, a decline in receipts owing to the recession and lower stock market value, tax cuts, and the expiration of the budget controls from the late 1990s. The publicly held debt-to-GDP ratio has ranged from 35 to 37 percent for most of this decade. The 2008 ratio of 40.8 percent is the highest since 1999, but is still far below the nearly 50 percent ratio of the mid-1990s.

The Long-Term Fiscal Outlook

While the Government's immediate priority is market stabilization and addressing the recession, it cannot lose sight of the longer term challenges. The Government's long-term financial condition will also depend on a number of factors, including: the market stabilization effort, the aging of the population and the growth rate of future health care costs. Consider the following:

- The 78 million baby boomers (those born between 1946 and 1964) comprise one quarter of the Nation's population. Beginning in 2008, the first of the 'boomers' became eligible for early retirement benefits under Social Security, and in 2011, they will start to become eligible for Medicare.
- Over the next 25 years, the share of the population aged 65 and older is forecast to *increase* from 12 percent to 20 percent (effectively increasing anticipated expenditures), while the share of the Nation's population that is working and paying taxes (anticipated revenue) will *decrease* from 60 percent to approximately 55 percent.
- Medicare spending has grown at more than 1½ times the overall rate of economic growth over the last four decades, and the Medicare Trustees assume that Medicare expenditures will continue to outpace overall economic growth in the future.
- Social Security, Medicare, and Medicaid expenditures are projected to grow from 44 percent of Government non-interest expenditures to 65 percent by 2030.
- Under current law, 30 years from now, Government revenues will be sufficient to cover approximately half of all anticipated expenditures.



- Chart B shows, as a percent of GDP, the Government's: (1) historical and assumed revenues (at 18 percent); (2) historical and projected long-term expenditures for Social Security, Medicare, Medicaid, interest on the debt held by the public, and other purposes, and (3) the difference between the two.[5]

The assumed constant revenue-to-GDP ratio of about 18 percent is based on an average historical ratio of 18 percent over the past several decades. Chart B also shows that, by 2080, expenditures on just three programs (Social Security, Medicare, and Medicaid) could absorb all Government revenue.

Without a change in law, by 2060, total Government expenditures are projected to be 45 percent of GDP– levels unseen since World War II, when Government expenditures reached a record high of 44 percent of GDP.

[5] In this chart, expenditures for Social Security and Medicare are consistent with the SOSI, expenditures for Medicaid reflect Medicare cost growth rates and Social Security demographic projections, and expenditures for all other programs and tax revenue are assumed to grow at the same rate of growth as GDP. Supplemental appropriations are assumed to be phased out over the next ten years.

And by 2080, expenditures could exceed 60 percent of GDP. Such a dramatic increase in spending and, as explained below, necessary Government borrowing is not sustainable.

Much uncertainty surrounds the future of Government programs and their impact on Government finances. Despite this uncertainty, projections such as these are critical to assessing whether future Government revenue will be sufficient to meet future expenses.

Social Insurance Trust Funds

Social Security:

- Old-Age and Survivors Insurance (OASI) pays retirement and survivors benefits,
- Disability Insurance (DI) pays disability benefits.

Medicare:

- Part A: Hospital Insurance (HI), which pays for inpatient hospital and related care.
- Part B: Supplementary Medical Insurance (SMI), which pays for physician and outpatient services
- Part D, SMI prescription drug benefit program.

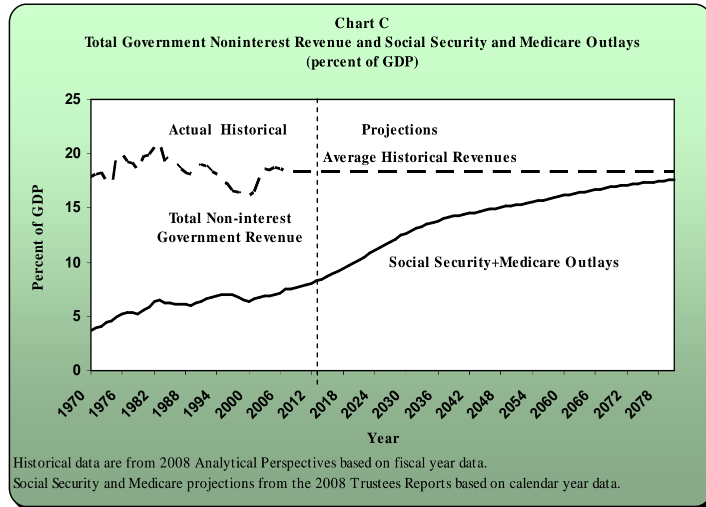
Social Insurance

For the 'social insurance' programs -- Social Security, Medicare, Railroad Retirement, and the Black Lung Program - the Statement of Social Insurance (SOSI) reports: (1) the actuarial present value of: all future program revenue (mainly taxes and premiums) - excluding interest - to be received from or on behalf of current and future participants; (2) the estimated future scheduled expenditures to be paid to or on behalf of current and future participants; and (3) the difference between (1) and (2). Amounts reported in the SOSI and in the supplemental information in this report are based on each program's official actuarial calculations.

Table 3: Social Insurance Future Expenditures in Excess of Future Revenues

	2008	2007	Increase (Decrease) $	%
Closed Group (Net):				
Social Security	$ 17,188	$ 16,265	$ 923	5.7%
Medicare:			$ -	
Part A	$ 13,590	$ 12,044	$ 1,546	12.8%
Part B	$ 12,615	$ 10,347	$ 2,268	21.9%
Part D	$ 5,605	$ 6,273	$ (668)	-10.6%
Subtotal - Medicare	$ 31,810	$ 28,664	$ 3,146	11.0%
Other	$ 137	$ 133	$ 4	2.7%
Total Social Insurance Expenditures, Net (Closed Group)	$ 49,135	$ 45,062	$ 4,073	4.9%
Total Net Social Insurance Expenditures, Net (Open Group)	$ 42,970	$ 40,948	$ 2,023	4.9%

The SOSI provides additional perspective on the Government's long term estimated exposures and costs. However, it should be noted that the Government's financial statements do not reflect future costs implied by any current policy, such as national defense, the global war on terrorism, and disaster relief and recovery. Table 3 shows the Government's estimated present value of future social insurance expenditures, net of dedicated future revenues for the programs reported in the Statement of Social Insurance (SOSI), projected to be $43 trillion as of January 1, 2008 for the 'Open Group'[6]. While these expenditures are currently not considered Government liabilities, they do have the potential to become liabilities in the future, based on the continuation of the social insurance programs' provisions contained in current law.



Historical data are from 2008 Analytical Perspectives based on fiscal year data.
Social Security and Medicare projections from the 2008 Trustees Reports based on calendar year data.

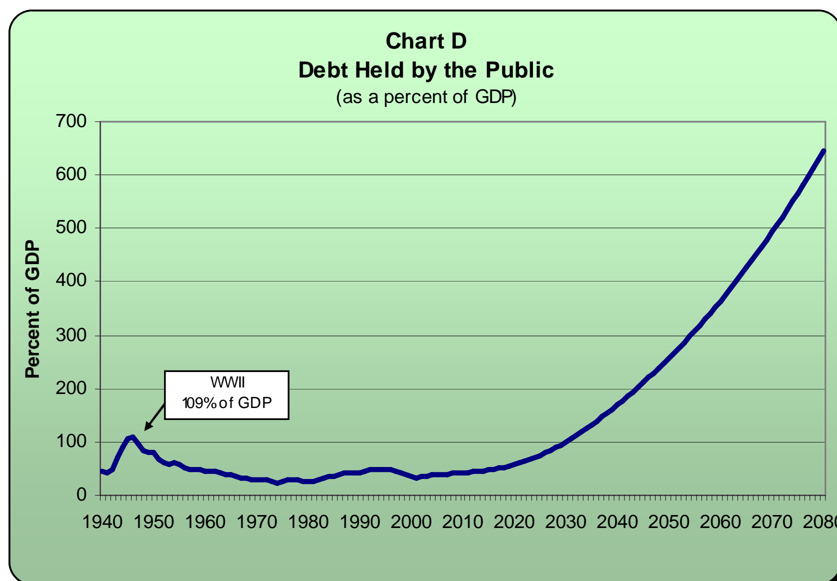
The social insurance trust funds account for all related program income and expenses. Social Security and Medicare taxes, premiums, and other income are credited to the funds; fund disbursements may only be made for benefit payments and program administrative costs. Any excess revenues (surpluses) are invested in special non-marketable U.S. Government securities at a market rate of interest. The trust funds represent the accumulated value, including interest, of all prior program surpluses, and provide automatic funding authority to pay for future benefits.

[6] 'Closed' Group and 'Open' Group differ by the population included in each calculation. From the SOSI, the 'Closed' Group includes: (1) participants who have attained eligibility and (2) participants who have not attained eligibility. The 'Open' Group adds future participants to 'Closed' Group. See 'Social Insurance' in the Supplemental Information section in this report for more information.

As shown in Chart C, over the next two decades, Medicare and Social Security expenditures are projected to increase from their current 8 percent of GDP to about 11 percent. By 2080, they are projected to be approaching the 18 percent of GDP assumed for all revenues[7]. Simply said, holding total revenues constant, current spending for Social Security and Medicare alone will put unsustainable pressure on limited Government resources.

Unsustainable Debt

As noted earlier, the Government must borrow from the public to finance any gaps between expenditures and revenues. Increased borrowing leads to higher levels of debt and debt service (net interest) which in turn can make it more difficult to balance expenditures and revenues in the future. Chart D shows that by 2017, publicly held debt is projected to rise to 50 percent of GDP, surpassing the non-wartime peak of 49 percent in 1993. Without changes to the major three entitlement programs, publicly held debt may be more than 110 percent of GDP by 2032, surpassing the World War II peak of 109 percent, and by 2080, publicly held debt may exceed 600 percent of GDP.



Such rapid growth in the Government's deficit and resulting debt would create financial sector instability, increasing risk and uncertainty across many sectors of the U.S. economy. Avoiding the economic consequences of this fiscal path will require action to bring program expenditures and Government resources in balance. Delays in addressing this critical issue could increase the magnitude of the changes needed and place a greater burden on future generations.

The Government has made and is expected to continue to make a vast commitment of financial resources to establish and maintain stability in the credit markets, although many of the financial assets acquired by the Government in its market stabilization efforts may eventually be sold and return value to the taxpayer. The Government has been able to take these stabilization actions because investors believe the United States' credit is unimpeachable, prompting investors to willingly purchase Treasury securities in preference to other securities. The unsustainable growth in Social Security, Medicare, and Medicaid remains a long-term fiscal challenge to be addressed once the current credit crisis has passed and overall economic conditions have improved.

[7] The Medicare Trustees' Report shows that, under current law, the Hospital Insurance Trust Fund will not have sufficient funds to pay scheduled benefits beginning in 2019. At that point, trust fund income would cover only 78 percent of scheduled benefits, falling to about 30 percent in 2082. The Social Security Trust Fund could encounter a similar problem. Under current law, trust fund income would cover only 78 percent of scheduled benefits in 2041 and only 75 percent in 2082.

Financial Position and Results of Operations

This *Report* provides the results of the Government's financial operations, including its financial condition, revenues and costs, assets and liabilities, and other obligations and commitments. This information, when combined with the President's Budget, collectively provides a valuable tool for managing current operations and planning future initiatives.

Accrual-Based Results and Basis of Accounting

Each year, the Administration issues two reports that detail financial results for the Federal Government: the *President's Budget*, whose main purpose is to provide a prospective discussion of future initiatives and the resources needed to support them; and this *Financial Report*, which provides the President, Congress, and the American people a broad, comprehensive overview of the cost on an accrual basis of the Government's operations, the sources used to finance them, its balance sheet, and the outlook for its social insurance programs.

President's Budget	Financial Report of the U.S. Government
Prepared primarily on a '*cash basis*' • Initiative-based: focus on current and future initiatives planned and how resources *will be used* to fund them. • Receipts ('cash in'), e.g. federal income tax received, National Park fees collected. • Outlays ('cash out'), e.g., defense spending, benefit checks sent.	Prepared on an '*accrual basis*' • Retrospective – prior and present resources used to implement initiatives. • Revenue: recognized when earned, but not necessarily received (with the exception of tax revenues - see footnote). • Costs: recognized when owed, but not necessarily paid.

Treasury prepares the financial statements in this Report on an 'accrual basis' of accounting as prescribed by U.S. generally accepted accounting principles (GAAP) for Federal entities.[8]

These standards are tailored to the Government's unique characteristics and circumstances. For example, agencies prepare a uniquely structured 'Statement of Net Cost,' which is intended to present net Government resources used in its operations, instead of an 'Income Statement,' which private sector companies typically use to focus on profits earned. Also unique to Government is the preparation of separate statements, to reconcile differences and articulate the relationship between budget and accrual accounting results (e.g., Statement of Reconciliation of Net Operating Revenue (or Cost) and Unified Budget Deficit and the Statement of Changes in Cash Balance from Unified Budget Deficit and Other Activities).

Reporting Entity

These financial statements conceptually cover the three branches of the Government (legislative, executive, and judicial). Legislative and judicial branch reporting focuses primarily on budgetary activity. Only executive branch entities are required, by law, to prepare audited financial statements. Some legislative branch entities do, however, voluntarily submit financial reports.

A number of Government entities and organizations are excluded due to the nature of their operations, including the Federal Reserve System (an independent entity that serves both public and private purposes); the Federal Retirement Thrift Investment Board; all fiduciary funds, and government-sponsored but privately-owned enterprises, including the Federal Home Loan Banks, the Federal National Mortgage Association, and the Federal Home Loan Mortgage Corporation. A list of the significant agencies and entities contributing to this report is included in the Appendices.

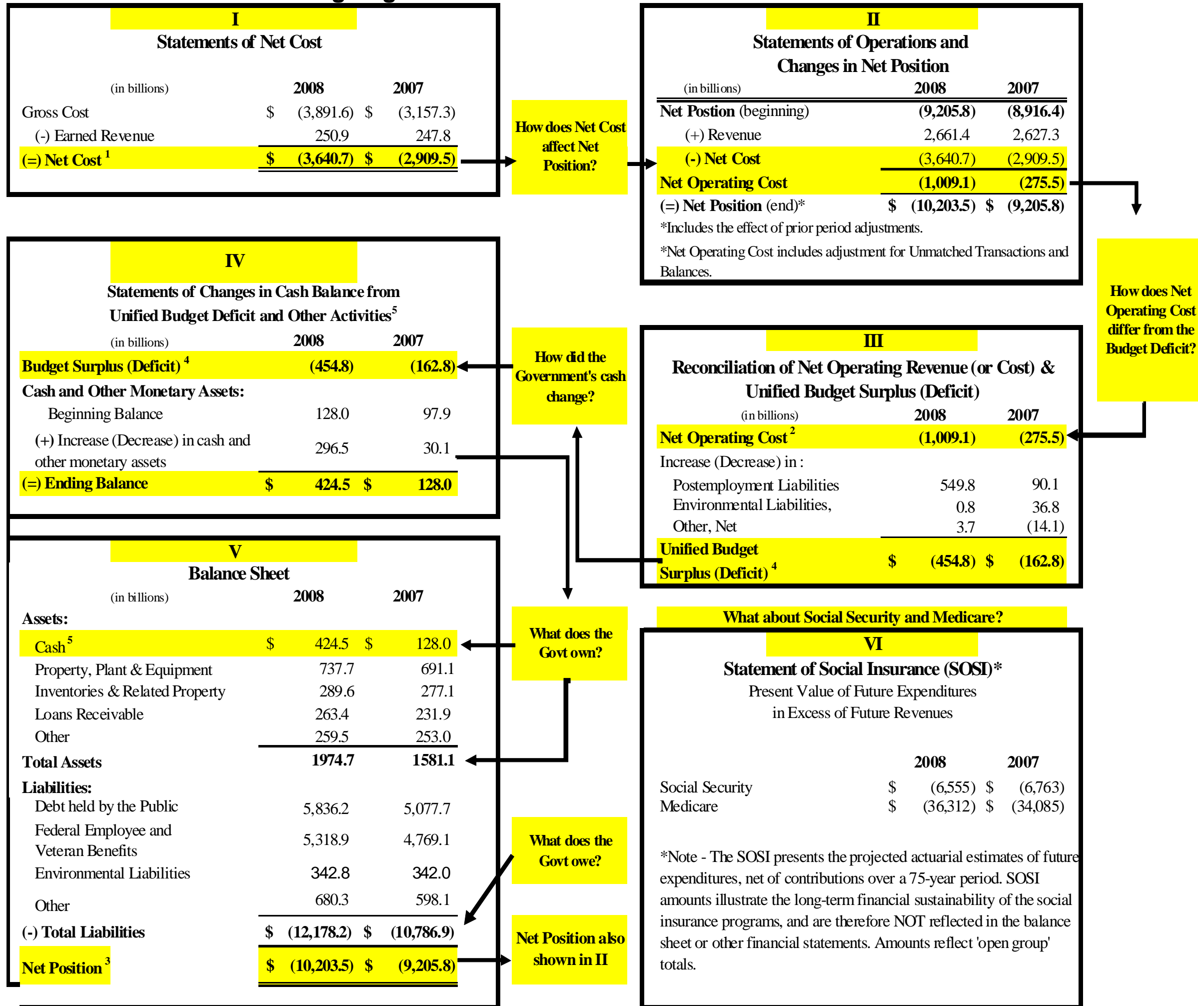
Limitations of the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the Federal Government, pursuant to the requirements of 31 U.S.C. § 331(e)(1). These statements are in addition to the financial reports used to monitor and control budgetary resources that are prepared from the same books and records.

Exhibit 3, on the following page is a blueprint to the Government's financial statements, demonstrating how they connect with one other.

[8] Under GAAP, most U.S. Government revenues are recognized on a 'modified cash' basis, or when they become measurable.

Exhibit 3
Navigating the Government's Financial Statements



I
Statements of Net Cost

(in billions)	2008	2007
Gross Cost	$ (3,891.6)	$ (3,157.3)
(-) Earned Revenue	250.9	247.8
(=) Net Cost [1]	**$ (3,640.7)**	**$ (2,909.5)**

II
Statements of Operations and Changes in Net Position

(in billions)	2008	2007
Net Postion (beginning)	**(9,205.8)**	**(8,916.4)**
(+) Revenue	2,661.4	2,627.3
(-) Net Cost	(3,640.7)	(2,909.5)
Net Operating Cost	**(1,009.1)**	**(275.5)**
(=) **Net Position** (end)*	**$ (10,203.5)**	**$ (9,205.8)**

*Includes the effect of prior period adjustments.

*Net Operating Cost includes adjustment for Unmatched Transactions and Balances.

III
Reconciliation of Net Operating Revenue (or Cost) & Unified Budget Surplus (Deficit)

(in billions)	2008	2007
Net Operating Cost [2]	**(1,009.1)**	**(275.5)**
Increase (Decrease) in :		
Postemployment Liabilities	549.8	90.1
Environmental Liabilities,	0.8	36.8
Other, Net	3.7	(14.1)
Unified Budget Surplus (Deficit) [4]	**$ (454.8)**	**$ (162.8)**

IV
Statements of Changes in Cash Balance from Unified Budget Deficit and Other Activities[5]

(in billions)	2008	2007
Budget Surplus (Deficit) [4]	**(454.8)**	**(162.8)**
Cash and Other Monetary Assets:		
Beginning Balance	128.0	97.9
(+) Increase (Decrease) in cash and other monetary assets	296.5	30.1
(=) Ending Balance	**$ 424.5**	**$ 128.0**

V
Balance Sheet

(in billions)	2008	2007
Assets:		
Cash [5]	$ 424.5	$ 128.0
Property, Plant & Equipment	737.7	691.1
Inventories & Related Property	289.6	277.1
Loans Receivable	263.4	231.9
Other	259.5	253.0
Total Assets	**1974.7**	**1581.1**
Liabilities:		
Debt held by the Public	5,836.2	5,077.7
Federal Employee and Veteran Benefits	5,318.9	4,769.1
Environmental Liabilities	342.8	342.0
Other	680.3	598.1
(-) Total Liabilities	**$ (12,178.2)**	**$ (10,786.9)**
Net Position [3]	**$ (10,203.5)**	**$ (9,205.8)**

What about Social Security and Medicare?

VI
Statement of Social Insurance (SOSI)*
Present Value of Future Expenditures in Excess of Future Revenues

	2008	2007
Social Security	$ (6,555)	$ (6,763)
Medicare	$ (36,312)	$ (34,085)

*Note - The SOSI presents the projected actuarial estimates of future expenditures, net of contributions over a 75-year period. SOSI amounts illustrate the long-term financial sustainability of the social insurance programs, and are therefore NOT reflected in the balance sheet or other financial statements. Amounts reflect 'open group' totals.

1. The Statements of Net Cost presents the Government's net operating expense, which, when combined with tax and other revenue in the Statement of Operations and Changes in Net Position, yields the Government's Net Operating Cost and shows how the Government's Net Position changed during the year.

2 The Net Position from the Statement of Operations and Changes in Net Position agrees to the Net Position on the Balance Sheet, which is based on the difference between the Government's reported assets and liabilities.

3. The 'Reconciliation Statement' shows the primary differences between the Government's accrual-based Net Operating Cost and cash-based unified budget deficit.

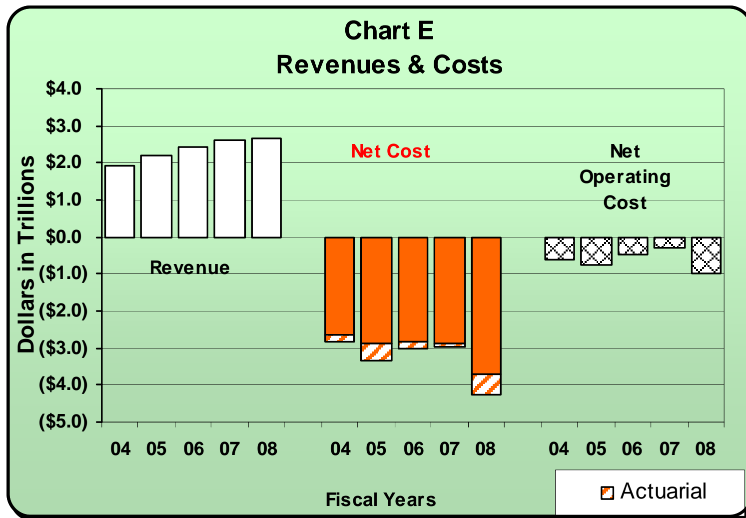
4 The Reconciliation of Net Operating Revenue (or Cost) and Unified Budget Surplus (or Deficit) shows the differences between the Government's spending deficit and its Net Operating Cost.

5 The Statement of Changes in Cash Balance from Unified Budget and Other Activities explains why the unified budget deficit normally would not result in an equivalent change in teh Government's Cash and Monetary Assets. The ending balance of Cash and Other Monetary Assets on this statement is the same as it is on the Balance Sheet.

Determining the Government's Net Position: "Where We Are"

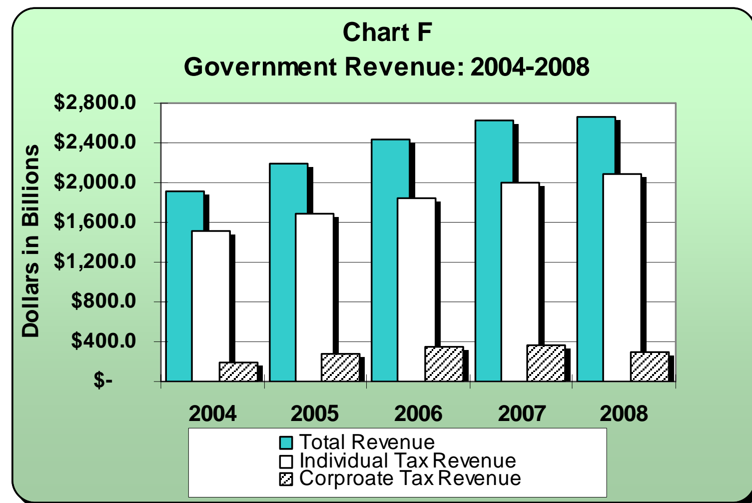
The Government's financial position and condition have traditionally been expressed through the Budget, focusing on the impact of surpluses and deficits. However, this primarily cash-based discussion of the Government's net outlays (deficit) or net receipts (surplus) tells only part of the story. The Government's net position is driven simultaneously by the Government's revenues and expenses, as well as the changes in its assets and liabilities.

Revenues and Costs: "What Came In & What Went Out"



The Government's ***Statement of Operations and Changes in Net Position***, much like a corporation's income statement, shows the Government's 'bottom line'. Chart E shows that the Government has incurred a total net operating cost (i.e., costs have exceeded its revenues) over the past several years. Notably, in FY 2008, net operating costs exceeded $1 trillion for the first time (Chart E). The Government's revenues last exceeded its costs in FYs 1999 and 2000 in concert with the budget surplus.

The Government nets its costs against both earned revenues from Government programs (e.g., national park entry fees) and taxes, which account for the vast majority of total revenues. In addition, the Government distinguishes revenues that are earmarked for specific purposes (e.g., Medicare premiums) from those for general purpose spending. The Government's 'bottom line' is its net operating cost, or total costs in excess of revenues. The Government must issue debt to finance any costs as they are paid that cannot be covered by revenues, subject to the statutory debt limit.



The ***Reconciliation of Net Operating Cost and Unified Budget Deficit Statement*** shows how the Government's net operating cost from the primarily accrual-based financial statements relates to the more widely-known cash-based budget deficit. Most of this difference is attributable to accruals of actuarial costs associated with the estimated present value of the Federal Government's net postemployment liabilities. Chart E shows the effect of this 'actuarial' element on the Government's total net cost. These actuarial costs, in recent years, have also accounted for majority of the change in the annual change in the Government's total net cots. The Department of Veterans Affairs (VA) and other agencies use a number of assumptions, such as interest rates and life expectancy, to make annual actuarial projections of their long-term benefits liabilities and the related costs. As further discussed later, changes in these assumptions can cause those projections, and consequently total costs, to fluctuate, sometimes significantly, year to year.

Revenue: "What Came In"

The ***Statement of Net Costs*** reports 'earned' revenue generated by Federal programs. In FY 2008, more than 25 percent of these revenues were attributable to Medicare premiums paid by program participants. The ***Statement of Operations and Changes in Net Position*** shows the Government's taxes and other revenues (i.e., revenues other than 'earned'). Government revenue totaled $2.7 trillion, remaining relatively constant and increasing slightly by $34 billion or just over 1 percent, compared to FY 2007. Individual income tax revenue increased by $79 billion or almost 4 percent. However, the developing recession precipitated a significant decline in corporate tax revenues ($67.5 billion or more than 18 percent). Individual and corporate tax revenue account for the majority (nearly 90 percent) of total revenues (see Chart F).

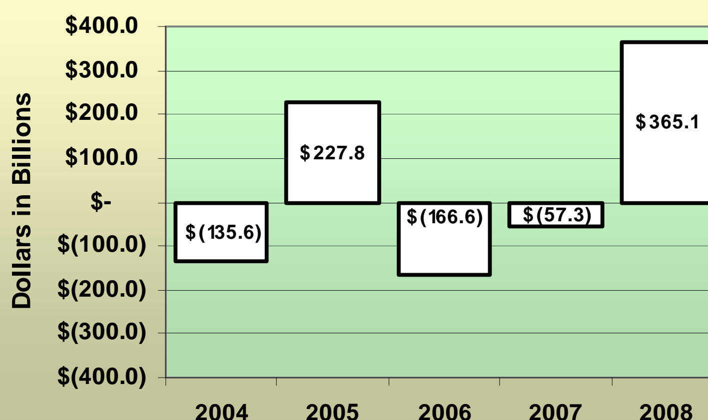
Table 4: Gross Cost. Revenues, and Net Cost

Dollars in Billions	2008	2007	Increase $	Increase %
Gross Cost				
DoD	$ (767.6)	$ (689.6)	$ (78.0)	11.3%
HHS	$ (769.1)	$ (718.6)	$ (50.5)	7.0%
SSA	$ (663.9)	$ (626.4)	$ (37.5)	6.0%
VA	$ (434.6)	$ (63.1)	$ (371.5)	588.7%
Interest on Federal Debt	$ (241.6)	$ (238.9)	$ (2.7)	1.1%
Other Federal Agencies	$ (1,014.8)	$ (820.7)	$ (194.1)	23.6%
Total Gross Cost	**($3,891.6)**	**($3,157.3)**	**$ (734.3)**	**18.9%**
Less: Earned Revenue	$250.9	$247.8	$ 3.1	1.2%
Net Cost	**($3,640.7)**	**($2,909.5)**	**$ (731.2)**	**25.1%**
Less: Taxes & Other Revenue	$ 2,661.4	$ 2,627.3	$ 34.1	1.3%
Net Operating Cost [1]	**($1,009.1)**	**($275.5)**	**$ (733.6)**	**266.3%**

[1] Net Operating Cost includes adjustment for Unmatched Transactions and Balances

Cost: "What Went Out"

The ***Statement of Net Cost*** also shows how much it costs to operate the Federal Government, recognizing expenses when they happen, regardless of when payment is made (accrual basis). It shows the derivation of the Government's net cost of operations or the difference between costs of goods produced and services rendered by the Government during the fiscal year. This amount, in turn, is offset against the Government's taxes and other revenue in the ***Statement of Operations and Changes in Net Position*** to calculate the 'bottom line' or net operating cost.



In FY 2008, the Government's 'bottom line' net operating cost totaled $1,009.1 billion or just over $1 trillion, a substantial increase over FY 2007's net operating cost of $275.5 billion (see Table 4). As noted earlier, changes in the actuarial calculations of VA's veterans benefit liability were the primary reason behind a nearly seven-fold increase in VA's actuarial and gross costs during FY 2008, compared with a relatively meager decrease in FY 2007 (see Chart G). Table 5 shows the major components of this significant liability change, which include changes in discount rates, pay adjustments, and estimates of veteran eligibility. The liability increase of $339 billion in FY 2008, when compared to a $26 billion decrease in FY 2007, combine to cause a $365 billion increase in actuarial cost for FY 2008. This was the largest increase by far at VA in recent years and accounted for: (1) approximately 98 percent of the increase in VA total net costs, and (2) about half of the increase in total net cost across the Government. DoD also experienced a significant increase ($110 billion) due to reestimation of its net postemployment benefit liabilities.

Table 5

Components of VA Federal Employee & Veteran Benefit Liability Change - FY 2008

Dollars in billions	$	%
Changes in discount rates	128	38%
Changes in original awards	106	31%
Change in report date	60	18%
Other sources	45	13%
Total Change	**339**	**100%**

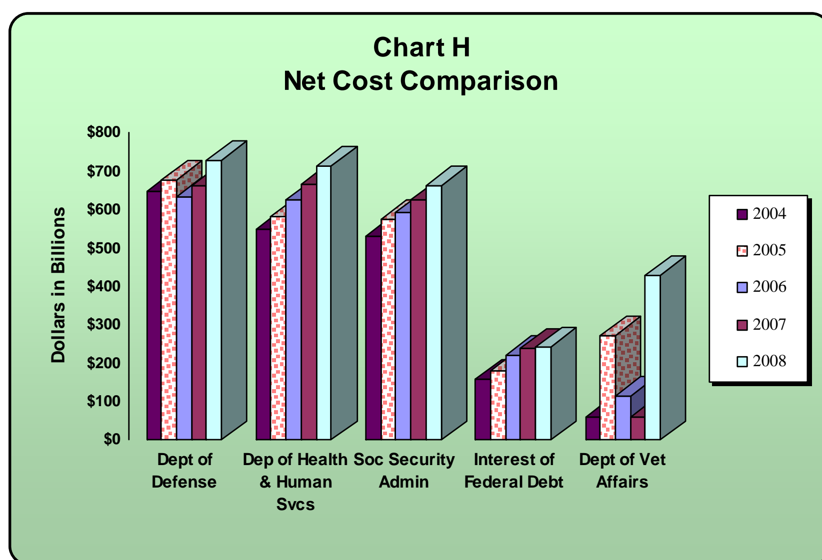


Chart H shows that DoD, HHS, and SSA have consistently incurred the largest agency shares of the Government's total net cost of operations in recent years. HHS and SSA combine to make up about 40 percent of the 2008 total net cost of operations, the bulk of which are attributable to these agencies' administration of the Government's major social insurance programs, e.g., Social Security and Medicare. The ***Statement of Social Insurance*** (SOSI) and the related information in this report discuss the current costs and future sustainability of these programs in greater detail. Of note, the substantial cost increase from VA's revaluation of net postemployment liabilities increased the Department's proportional share of total net costs from 2 percent in FY 2007 to 12 percent in FY 2008. Among cabinet agencies, the Energy Department experienced the greatest cost decrease (50 percent). Energy also attributes the majority of this decrease to revaluations of unfunded liability estimates, caused primarily by a 1.25 percentage point increase in the discount rate and smaller than expected pension plan values.

Assets and Liabilities: "What We Own and What We Owe"

Net Position at the end of the year can also be derived by netting the Government's assets against its liabilities, as presented in the ***Balance Sheet***. It is important to note that the balance sheet does not include the financial value of the Government's sovereign powers to tax, regulate commerce, and set monetary policy. It also excludes its control over nonoperational resources, including national and natural resources, for which the Government is a steward. As noted earlier, the Government distinguishes between resources and spending that are earmarked for specific purposes versus those intended for general purposes. In FY 2008, earmarked funds accounted for less than 6 percent of the Government's total Net Position. In addition, as was the case with the ***Statement of Operations and Changes in Net Position***, the ***Balance Sheet*** does include a separate presentation of the portion of net position earmarked for specific funds and programs (e.g., Social Security, Medicare, unemployment, and military and civilian retirement). Moreover, the Government's exposures are broader than the liabilities presented on the balance sheet, including such items as the Government's future social insurance exposures (e.g., Social Security and Medicare), as well as other commitments and contingencies. These exposures are discussed in this section as well as in the supplemental disclosures of this Report.

Table 6: Assets and Liabilities

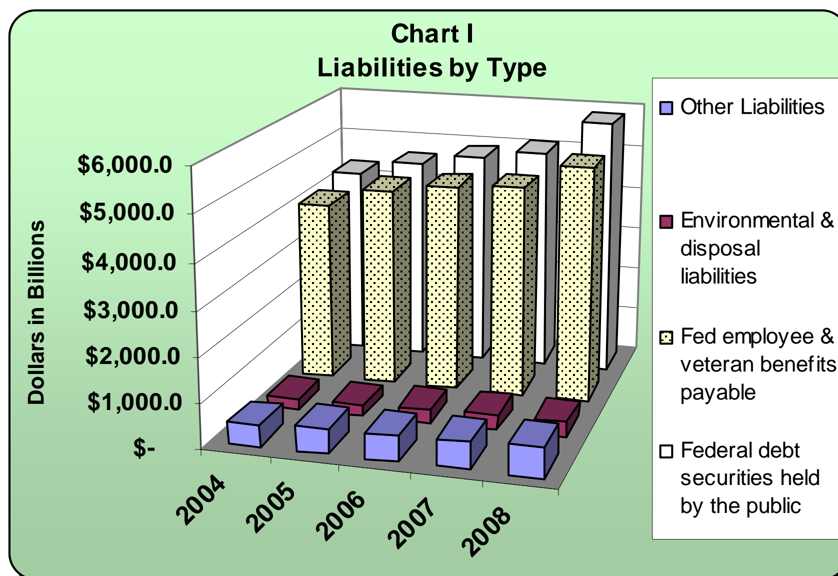
Net Position Dollars in Billions	**2008**	**2007**	Increase (Decrease) **$**	 **%**
Assets	**$ 1,974.7**	**$ 1,581.1**	$ 393.6	24.9%
Less: Liabilities, comprised of:				
Debt Held by the Public	$ 5,836.2	$ 5,077.7	$ 758.5	14.9%
Federal Employee & Veterans Benefits	$ 5,318.9	$ 4,769.1	$ 549.8	11.5%
Other Liabilities	$ 1,023.1	$ 940.1	$ 83.0	8.8%
Total Liabilities	**$ 12,178.2**	**$ 10,786.9**	$ 1,391.3	12.9%
Net Position (Assets Minus Liabilities)	**$ (10,203.5)**	**$ (9,205.8)**	**$ (997.7)**	**-10.8%**

Assets – "What We Own"

During FY 2008, nearly all Government asset balances increased. Net property, plant, and equipment ($737.7 billion in FY 2008) has been the Government's largest asset over the past several fiscal years, accounting for approximately 40% percent of $1,974.7 billion in total assets in FY 2008 (see Table 6). As part of the market stabilization effort, the Government implemented the Supplementary Financing Program (SFP) - a temporary program that deposits cash in Treasury bank accounts with the Fed -- causing the Government's cash balance to rise by $300 billion as of September 30, 2008. This program also accounted for a corresponding $300 billion increase in publicly held debt. In addition to assets recorded on the balance sheet, the Government owns certain other stewardship assets such as land (e.g., national parks and forests) and heritage assets (e.g., national memorials and historic structures).

Liabilities – "What We Owe"

Chart I shows the major components of liabilities, or what the Government owes, as of September 30, for fiscal years 2004 through 2008. As indicated in Table 6, the largest liability in recent years has been Federal debt held by the public and accrued interest, the balance of which increased to $5,836.2 billion in FY 2008. The increase in expenditures resulted in the Government having to borrow additional cash from the public this year. In addition, as noted above, implementation of the temporary SFP resulted in the issuance of hundreds of billions of dollars in new debt. Over the past seven fiscal years, Federal debt securities held by the public and accrued interest have moved in tandem with the budget results. ***The Statements of Changes in Cash Balance from Unified Budget and Other Activities*** reports how the annual unified budget surplus or deficit relates to the Federal Government's borrowing and changes in cash and other monetary assets, and explains how a budget surplus or deficit normally affects changes in debt balances.



The Government's net borrowings from the public, including accrued interest, increased by $758.5 billion in FY 2008. Typically, budget surpluses have resulted in borrowing reductions, and budget deficits have yielded borrowing increases. However, the Government's debt operations are much more complex than this would imply. Each year, trillions of dollars of debt matures and new debt takes its place. In FY 2008, new borrowings were $5.6 trillion and maturing debts repaid were $4.9 trillion. As noted earlier, market stabilization efforts could further impact net borrowings as the Government will likely need to issue debt to continue to fund financial asset purchases and support the capital needs of the banking industry.

Federal employee postemployment and veteran benefits payable have increased dramatically in recent years, to $5,318.9 billion as of fiscal year-end 2008 (representing nearly half of the Government's total liabilities), with civilian benefits payable accounting for more than a third of total employee and veteran benefits. The Office of Personnel Management (OPM) administers the largest civilian pension plan, covering nearly 2 million current employees and 2.4 million annuitants[9]. The military pension plan covers nearly 3 million current employees (including active service, reserve, and national guard) and approximately 2.2 million annuitants[10]. Environmental and disposal liabilities stayed relatively constant at approximately $343 billion as of September 30, 2008. The majority of these types of liabilities are attributable to the Departments of Defense and Energy for the clean-up of radioactive waste and other nuclear material stored at former testing and storage sites.

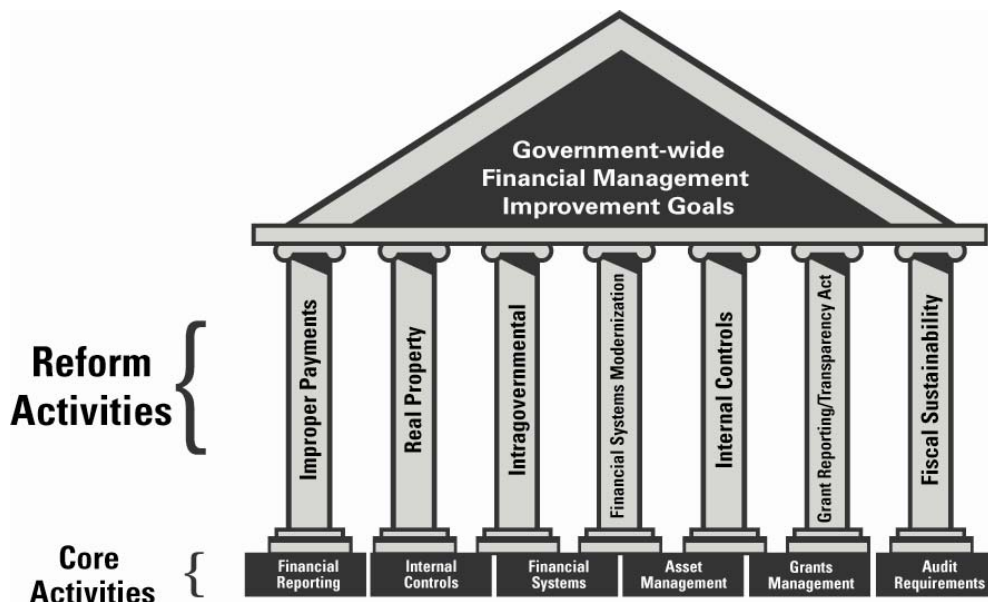
[9] OPM FY 2008 Performance and Accountability Report, p. 1.

[10] DoD FY 2008 Military Retirement Fund (MRF) financial statements, p 6.

How We Define and Measure Financial Management Success

The Office of Management and Budget (OMB) provides Federal agencies with a concise set of clear and measurable financial management performance goals that allow Federal managers, Congress, and the public to gauge whether taxpayer funds are being properly accounted for and wisely spent. These performance measures include, among others, the achievement of clean audit opinions, the elimination of material weaknesses in internal control, timely financial reporting, the disposal of excess real property, the elimination of improper payments, and the reduction in government costs through the strategic use of financial data. What follows is an overview of FY 2008 results for OMB's Government-wide initiatives: 1) Improving Financial Performance, 2) Eliminating Improper Payments, and 3) Real Property Asset Management.[11]

These initiatives are managed by OMB's Office of Federal Financial Management (OFFM). OFFM has also developed a "Framework for Improving Financial Performance" to provide direction and clarity on how these financial management improvement goals will be met. The Framework (as depicted in the below diagram) is intended to provide stakeholders with a simple tool for identifying the: 1) priority objectives of the Government's financial management improvement efforts, which historically have included improving financial statement audit results and other financial health metrics, such as reducing improper payments; 2) ongoing Government-wide financial management reform activities; and 3) day-to-day financial management activities or "core" activities that help ensure a strong foundation is in place for achieving financial management success.



The Framework is also described in OFFM's 2008 Federal Financial Management Report that was submitted to the Congress on January 31, 2008. The most recent reports are available at http://www.whitehouse.gov/omb/financial/reports. Also visit http://www.Results.gov and http://www.ExpectMore.gov for additional information on OMB's initiatives, including individual agencies' performance under these initiatives, and agencies' performance under their individual programs.[12]

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11 The other four initiatives are: 1) Implementing Strategic Human Capital, 2) Gaining Efficiencies through Strategic Sourcing, 3) Expanding Electronic Government, and 4) Performance Improvement.

12 Since programs are not administered at the Government-wide level, the FASAB requirement to report performance goals and measures for the Federal Government as a whole does not apply and, therefore, is not reported upon here. Program administration and the subsequent reporting of the outcomes and results of those programs are handled at the agency level.

Fiscal Year 2008 Results

Improving Financial Performance

For the fourth year in a row, **all** major Federal agencies successfully met the 45-day financial audit deadline as required by the rigorous reporting guidelines set by OMB. Since 2004, agencies are required to complete the financial report 45-days after the end of the fiscal year, compared to the previous five month (150 days) window for completion. The accelerated deadline results in more immediate availability of financial information to agency decision-makers and requires agencies to employ rigorous disciplines throughout the year to ensure readiness for year-end reporting.

In addition to timely reporting, the results from FY 2008 show that the Federal Government is improving the validity of its financial information. Of the 24 major Federal agencies, 20 received clean opinions, one more than the 19 clean opinions reported last year and the highest total in the past 6 years. Table 7 below includes the audit results for FY 2008.

Table 7: Summary of FY 2008 Financial Statement Results by Agencies

CFO Act Agencies:	*FY 2008 Audit Opinion*
Department of Agriculture (USDA)	Unqualified
Department of Commerce (DOC)	Unqualified
Department of Defense (DOD)	Disclaimer
Department of Education (Education)	Unqualified
Department of Energy (DOE)	Unqualified
Department of Health and Human Services (HHS)	Unqualified
Department of Homeland Security (DHS)[13]	Disclaimer
Department of Housing and Urban Development (HUD)	Unqualified
Department of the Interior (DOI)	Unqualified
Department of Labor (DOL)	Unqualified
Department of Justice (DOJ)	Unqualified
Department of State (State)	Disclaimer
Department of Transportation (DOT)	Unqualified
Department of the Treasury (Treasury)	Unqualified
Department of Veterans Affairs (VA)	Unqualified
Agency for International Development (USAID)	Unqualified
Environmental Protection Agency (EPA)	Unqualified
General Services Administration (GSA)	Unqualified
National Aeronautics and Space Administration (NASA)	Disclaimer
National Science Foundation (NSF)	Unqualified
Nuclear Regulatory Commission (NRC)	Unqualified
Office of Personnel Management (OPM)	Unqualified
Small Business Administration (SBA)	Unqualified
Social Security Administration (SSA)	Unqualified

This year's Government-wide results are complemented by notable milestones for these individual agencies:

[13] Balance Sheet and Custodial Statement Audit Only

- **The U.S. Army Corps of Engineers (USACE).** USACE achieved its first ever clean audit opinion. The Army Corps is the largest organization within the Department of Defense (DoD) to achieve this milestone. This accomplishment is a critical building block for DoD's overarching effort to achieve a clean opinion.

- **The Department of the Treasury (Treasury).** As the Federal government took action to stabilize the economy, the Treasury faced the challenge of accounting for an unprecedented and complex array of financial activities that took place within a few days of the end of the fiscal year. The Treasury Department's achievement of a clean audit opinion this year demonstrates that it was equal to the financial reporting challenge posed by the new programs undertaken to address the economic crisis.

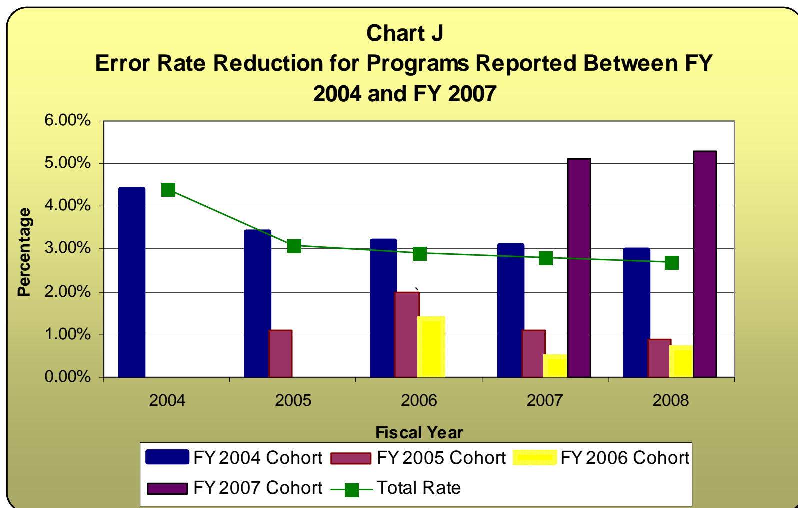
- **The Department of Transportation (DOT).** DOT, for the first time in its history, achieved a clean opinion with no material weaknesses. DOT joins the ranks of the Departments of Justice and Housing and Urban Development as one of the Government's larger and more complex Federal agencies to achieve the important milestone of a clean opinion with no material weaknesses.

In addition to these results, the total number of material weaknesses Government-wide declined from 39 to 32 (or 18 percent), primarily from a reduction in Financial Systems and Security material weaknesses. The remaining 32 material weaknesses are primarily comprised of weaknesses related to Financial Management and Reporting, Financial Systems and Security, Property, Plant & Equipment (PP&E), and Budgetary Reporting. Examples of these weaknesses entail improvements needed in controls over: the financial statement preparation process, Information Technology security, the receipt and tracking of PP&E, and funds control. This is the fifth year in a row that material weaknesses have declined, with almost a 50 percent decrease in weaknesses since 2001.

Eliminating Improper Payments

Fiscal Year 2008 was also an important year for identifying, measuring, and eliminating improper payments (e.g., the right amount, to the right recipient). Full transparency of annual improper payment totals allows the public to understand the extent of payment errors and assess the Government's efforts to eliminate them. With this year's financial reports, Federal agencies are now reporting improper payment measurements for nearly 95 percent of all high-risk programs (up from 85 percent in FY 2007), with error rates reported on 12 new programs, including Medicaid and parts of the Medicare program.

The results from the past five years of reporting on improper payments demonstrate that once an agency has measured and reported program errors, it is able to implement corrective actions to reduce those errors in subsequent years. As illustrated in Chart J,[14] Error Rate Reduction for Programs Reported Between FY 2004 and FY 2007, the error rate for the first programs measured, in FY 2004, was 4.4 percent (or $45.1 billion in improper payments). For these programs, the error rate has declined to 3.0 percent (or a $7.1 billion reduction in improper payments). Similar to the progress achieved in programs that first reported in FY 2004, programs that first reported in FYs 2005, 2006, and 2007 have reduced improper payments, representing an $800 million reduction.[15]



With 12 additional programs reporting in FY 2008, the preliminary Government-wide error rate is 3.9 percent or $71.7 billion, an increase of $16.7 billion from FY 2007. The increase is driven primarily by the newly measured programs, which include parts of Medicare and Medicaid. A significant cause of improper payments is insufficient

14 The table does not include programs reporting for the first time in FY 2008.

15 In FY 2007, Medicaid measured one of its components and reported an 18.4 percent error rate. In FY 2008, Medicaid measured all program components and reported a 10.5 percent error rate. For IPIA reporting, Medicaid will be reported in the FY 2008 cohort.

documentation, meaning that all of the supporting documentation necessary to verify the accuracy of the claim was not provided. If all the supporting documentation had been received, the agencies could have better determined whether the payment was appropriate or made in error. As documentation of payments improves, it is anticipated that the amount of payment errors reported will decline significantly.

Asset Management

Under the OMB's Real Property Asset Management initiative, agencies continue to make significant progress implementing the necessary tools to manage the size, condition, and costs of their asset portfolios and comply with Executive Order 13327, Federal Real Property Asset Management. In FY 2008, Executive agencies reported more than 1.1 million assets, including land, buildings, and structures, to the Government-wide real property inventory. This resource provides a more complete picture of the Government's asset inventory; where the assets are located; and how and whether the assets are used effectively to serve agencies' missions and objectives, than was previously possible. A more complete inventory picture and performance information ensures that agencies, and the Government as a whole, can make smarter asset management decisions. Agencies are also using this information to move forward with efforts to improve asset condition, increase asset utilization, and dispose of unneeded assets.

OMB continues holding agencies accountable for their asset management goals through the Real Property Asset Management process. Since FY 2004, agencies have significantly improved their asset management processes and their ability to gather and use inventory and performance data to drive the decision-making process toward rightsizing the Government's real property assets. To this end, Executive agencies have disposed of more than $8 billion in real property assets and are well on the way to meeting OMB's goal of disposing $9 billion in assets by the close of FY 2009.

Systems, Controls, & Legal Compliance

Systems

As Federal agencies demonstrate success in obtaining and keeping an unqualified opinion on their audited financial statements, the Federal Government continues to face challenges in implementing financial systems that meet Federal requirements. Although the number of agencies in compliance with the Federal Financial Management Improvement Act (FFMIA) continued to increase in fiscal year 2008 from 14 to 15, the number of auditors reporting compliance with FFMIA decreased from 11 to 10. The annual changes in compliances reported each year underscores the importance of current initiatives to standardize the financial management practices across the Federal Government.

In addition, OMB has continued to standardize common business processes across the Government, create opportunities for agencies to move financial systems to shared service providers, and increase transparency by establishing performance measures to evaluate the results. These efforts will help agencies implement financial systems that are compliant with Federal requirements and improve the cost, quality, and performance in the Government's financial management systems.

This year, OMB will be updating Circular No. A-127, *Financial Management Systems*. The revised Circular will clarify the definition of FFMIA substantial compliance so that auditors and agency heads interpret the guidance more consistently. This effort will further improve management of financial systems.

Controls

Federal managers have a fundamental responsibility to develop and maintain effective internal control. Effective internal control helps to ensure that programs are managed with integrity and resources are used efficiently and effectively through three objectives: effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations. The safeguarding of assets is a subcomponent of each objective.

The OMB Circular No. A-123 is the policy document that implements the requirements of the Federal Managers' Financial Integrity Act (FMFIA). Circular No. A-123 primarily focuses on providing agencies with a framework for assessing and managing risks more strategically and effectively. The Circular contains multiple appendices that address, at a more detailed level, one or more of the objectives of effective internal control. Appendix A provides a methodology for agency management to assess, document, test, and report on the internal control over financial reporting. Appendix B requires agencies to maintain internal control that reduces the risk of fraud, waste, and error in government charge card programs. Appendix C implements the requirements of the Improper Payment Information Act, which includes the measurement and remediation of improper payments.

Law & Policy	What it Does
Federal Managers' Finanical Integrity Act of 1982	requires the head of each executive agency to annually prepare a statement reporting the effectiveness of the agency's internal control and whether its systems comply with the federal financial system requirements.
Federal Financial Management Improvement Act of 1996	requries that Federal financial management systems provide accurate, reliable, and timely financial management information to the Government's managers.
OMB Circular A-123	provides instruction to agencies for implementing the **FMFIA**
OMB Circular A-127	provides instruction for complying with the federal financial system requirements.

In FY 2008, agencies continued to implement the requirements of FMFIA and Circular No. A-123 and have made much progress. The 24 major CFO Act agencies completed the third year of the more rigorous assessment of the internal control over financial reporting as required by the A-123 Appendix A. This year, 22 of the 24 major CFO Act agencies completed a full scope Appendix A assessment of the internal control over financial reporting (testing all key processes) as compared to 17 agencies last year. During FY 2009, OMB will continue working with the remaining two agencies that have not yet completed the full scope assessment. During FY 2008, OMB facilitated a forum on the better integration and leverage of internal control reviews being performed throughout departments and agencies through the exploration of alternate frameworks and implementation strategies. The forum included representatives from the financial, audit, acquisition, program, and information technology communities. Due to the myriad of legislative and regulatory requirements, internal control reviews, to satisfy those legislative and regulatory requirements, have been layered upon each other rather than being integrated. This forum included a robust discussion of alternatives and current practices that will inform potential next steps in future guidance.

This year, OMB will be updating Circular No. A-123, Appendix B. The revised appendix will expand the scope to include convenience checks, introduce a disciplinary framework for charge card abuse, and discuss the accounting for property purchased with charge cards.

Pursuant to Circular No. A-123, Appendix C, Federal agencies are now reporting improper payment measurements for nearly 95 percent of all high-risk outlays and reported error rates for 12 new programs (see Eliminating Improper Payments section for more details).

While many agencies are making progress identifying and resolving deficiencies found in internal control, continued diligence and commitment are needed. However, effective internal control is not only a challenge at the agency level, but it is also a challenge at the Government-wide level. Consequently, GAO has issued an adverse opinion on the effectiveness of the internal control for the Government as a whole, in its report.

Legal Compliance

Federal agencies are required to comply with a wide range of laws and regulations, including appropriations, employment, health and safety, and others. Responsibility for compliance primarily rests with agency management. Compliance is addressed as part of agency financial statement audits. Agency auditors test for compliance with selected laws and regulations related to financial reporting. Certain individual agency audit reports contain instances of noncompliance. None of these instances were material to the Government-wide financial statements. However, GAO reported that its work on compliance with laws and regulations was limited by the material weaknesses and scope limitations discussed in its report.

Additional Information

This *Financial Report's* Appendix contains the names and websites of the significant Government entities included in the Report's financial statements. Details about the information in this *Financial Report* can be found in these entities' financial statements included in their Performance and Accountability and Annual Financial Reports. This *Financial Report*, as well as those from previous years, are also available at the Treasury, OMB, and GAO websites at: http://www.fms.treas.gov/fr/index.html; http://www.whitehouse.gov/omb/financial/index.html; and www.gao.gov, respectively. Other related Government publications include, but are not limited to the:

- *Budget of the United States Government*,
- *Treasury Bulletin*,
- *Monthly Treasury Statement of Receipts and Outlays of the United States Government*,
- *Monthly Statement of the Public Debt of the United States*,
- *Economic Report of the President*, and
- *Trustees' Reports* for the Social Security and Medicare Programs.

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Comptroller General of the United States

United States Government Accountability Office
Washington, DC 20548

December 15, 2008

The President
The President of the Senate
The Speaker of the House of Representatives

The need for reliable, high-quality financial information has never been greater. However, our report illustrates that much work remains to be done on improving the state of federal financial management. Continued improvement needs to be a top priority of the new administration and Congress to help provide the financial accountability the public deserves and the information decision makers need to help evaluate government programs and manage the government in a cost-effective manner.

Our report on the U.S. government's consolidated financial statements for fiscal years 2008 and 2007 is enclosed. In summary we found the following:

- Certain material weaknesses in financial reporting and other limitations on the scope of our work resulted in conditions that prevented us from expressing an opinion on the financial statements other than the 2008 and 2007 Statements of Social Insurance. About $847 billion, or 43 percent, of the federal government's reported total assets as of September 30, 2008, and approximately $833 billion, or 23 percent, of the federal government's reported net cost for fiscal year 2008 relate to four of the Chief Financial Officers (CFO) Act agencies' fiscal year 2008 financial statements that, as of the date of our report, received disclaimers of opinion or were not audited.[1]
- The 2008 and 2007 Statements of Social Insurance are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles; we disclaim an opinion on the 2006 Statement of Social Insurance.[2]
- The federal government did not maintain effective internal control over financial reporting (including safeguarding assets) and compliance with significant laws and regulations as of September 30, 2008.

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[1]Of the 24 CFO Act agencies, the agencies that, as of the date of our report, received disclaimers of opinions on all of their fiscal year 2008 financial statements were the Department of Defense, Department of State, and the National Aeronautics and Space Administration. For the Department of Homeland Security for fiscal year 2008, only the Consolidated Balance Sheet and the Statement of Custodial Activity were subjected to audit; the auditor was unable to express an opinion on these two financial statements.
[2]Beginning in fiscal year 2006, the Statement of Social Insurance became a principal financial statement and was audited as part of the applicable federal agencies' financial statements. We disclaimed an opinion on the fiscal year 2006 consolidated financial statements, including the Statement of Social Insurance.

- Our work to test compliance with selected provisions of significant laws and regulations in fiscal year 2008 was limited by the material weaknesses and scope limitations discussed in our report.

While significant progress has been made in improving financial management since the federal government began preparing consolidated financial statements 12 years ago, three major impediments have continued to prevent us from rendering an opinion on the accrual basis consolidated financial statements over this period of time:[3] (1) serious financial management problems at the Department of Defense, (2) the federal government's inability to adequately account for and reconcile intragovernmental activity and balances between federal agencies, and (3) the federal government's ineffective process for preparing the consolidated financial statements. In addition to the material weaknesses underlying these major impediments, we noted three material weaknesses involving the federal government's inability to (1) determine the full extent to which improper payments occur and reasonably assure that appropriate actions are taken to cost-effectively reduce improper payments, (2) identify and resolve information security control deficiencies and manage information security risks on an ongoing basis, and (3) effectively manage its tax collection activities. Until the problems outlined in our audit report are adequately addressed, they will continue to have adverse implications for the federal government and American taxpayers.

The material weaknesses discussed in our report continued to (1) hamper the federal government's ability to reliably report a significant portion of its assets, liabilities, costs, and other related information; (2) affect the federal government's ability to reliably measure the full cost as well as the financial and nonfinancial performance of certain programs and activities; (3) impair the federal government's ability to adequately safeguard significant assets and properly record various transactions; and (4) hinder the federal government from having reliable financial information to operate in an efficient and effective manner.

The federal government is taking unprecedented actions to restore stability to financial markets, including specific actions in fiscal year 2008 to address capital and liquidity problems at the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac), which together held or guaranteed approximately $5 trillion of mortgages and mortgage-backed securities as of September 30, 2008. In addition, legislation enacted early in fiscal year 2009 authorized the creation of the Troubled Asset Relief Program (TARP) that enables the federal government to purchase or insure certain troubled assets that it deems necessary to promote financial

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[3]The accrual basis consolidated financial statements for the fiscal years ended September 30, 2008 and 2007 consist of the (1) Statements of Net Cost, (2) Statements of Operations and Changes in Net Position, (3) Reconciliations of Net Operating Cost and Unified Budget Deficit, (4) Statements of Changes in Cash Balance from Unified Budget and Other Activities, and (5) Balance Sheets, including the related notes to these financial statements. Most revenues are recorded on a modified cash basis. The 2008 and 2007 Statements of Social Insurance, including the related notes, are also included in the consolidated financial statements. The Statements of Social Insurance do not interrelate to the accrual basis consolidated financial statements.

market stability.[4] Under TARP, the federal government has injected billions of dollars into certain financial institutions. These and other actions the federal government has taken to stabilize financial markets and restore the availability of credit for Americans are discussed in this *2008 Financial Report of the United States Government*. These actions will likely have a significant effect on the federal government's financial condition, at least in the short-term, through increased borrowing. In addition, the current recession could significantly affect the federal government's future tax revenues and the value of certain of its assets and liabilities.

Currently, policymakers are understandably focused on dealing with stabilizing financial markets and stimulating the economy. However, once these issues are addressed, the nation's new and returning leaders will need to turn their attention to the long-term challenges of addressing the federal government's large and growing structural deficits that are driven primarily by rising health care costs and known demographic trends. As discussed in this *2008 Financial Report of the United States Government*, the federal government is on an unsustainable long-term fiscal path. The Statement of Social Insurance, for example, shows that projected scheduled benefits exceed earmarked revenues for social insurance programs (e.g., Social Security and Medicare) by approximately $43 trillion[5] in present value terms over the 75-year projection period. GAO also prepares long-term fiscal simulations that are based on the Social Security and Medicare Trustees' projections, but provide a more comprehensive analysis of fiscal sustainability because they include revenue and expenditure projections for all other government programs. Our most recent long-term fiscal simulation was issued in September 2008.[6]

Accounting and financial reporting standards have continued to evolve to provide greater transparency and accountability over the federal government's operations, financial condition, and fiscal outlook. However, further enhancements to accounting and financial reporting standards are needed to more effectively convey the long-term financial condition of the federal government and annual changes therein. For example, it should include a Statement of Fiscal Sustainability[7]—providing information on the long-term sustainability of social insurance programs in the context of all federal programs—and other sustainability information, including intergenerational equity and an analysis of changes in sustainability during the year.[8, 9] In addition, there is a need for a combined report on the performance and financial accountability of the federal government as a

[4]The TARP was established by the Department of the Treasury under authority provided in the Emergency Economic Stabilization Act of 2008 (Pub. L. No. 110-343).
[5]On an open group basis (current and future participants).
[6]GAO, *The Nation's Long-Term Fiscal Outlook: September 2008 Update*, GAO-09-94R (Washington, D.C.: September 2008).
[7]The Statement of Fiscal Sustainability would show the relationship between the present value of projected revenues and outlays for social insurance and for all other federal programs.
[8]Intergenerational equity assesses the extent to which different age groups may be required to assume financial burdens to sustain federal responsibilities.
[9]On September 2, 2008, the Federal Accounting Standards Advisory Board (FASAB) issued an exposure draft concerning long-term fiscal sustainability, *Reporting Comprehensive Long-Term Fiscal Projections for the U.S. Government*; and on November 17, 2008, an exposure draft was issued concerning accounting for social insurance, *Accounting for Social Insurance, Revised*.

whole. This report would include, among other things, key outcome-based national indicators (e.g., economic, security, social, and environmental), which could be used to help assess the nation's and other governmental jurisdictions' position and progress.

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This report would not be possible without the commitment and professionalism of Inspectors General throughout the federal government who are responsible for annually auditing the financial statements of individual federal agencies. We also appreciate the cooperation and assistance of the Department of the Treasury and Office of Management and Budget officials, as well as the federal agencies' CFOs. We look forward to continuing to work with these individuals, the new administration, and the Congress to achieve the goals and objectives of financial management reform.

Our audit report begins on page 165. Our guide[10] to the *Financial Report of the United States Government* is intended to help those who seek to obtain a better understanding of the *Financial Report.* In addition, our guide[11] on *Understanding Similarities and Differences between Accrual and Cash Deficits* provides a useful perspective on the different purposes cash and accrual measures serve in providing a comprehensive picture of the federal government's fiscal condition today and over time. These guides are available on GAO's Web site at www.gao.gov.

Our report was prepared under the direction of Robert F. Dacey, Chief Accountant, and Gary T. Engel, Director, Financial Management and Assurance. If you have any questions, please contact me on (202) 512-5500 or them on (202) 512-3406.

Gene L. Dodaro
Acting Comptroller General
of the United States

cc: The Majority Leader of the Senate
The Minority Leader of the Senate
The Majority Leader of the House
The Minority Leader of the House

(198521)

[10]GAO, *Understanding the Primary Components of the Annual Financial Report of the United States Government*, GAO-05-958SP (Washington, D.C.: September 2005).
[11]GAO, *Understanding Similarities and Differences between Accrual and Cash Deficits*, GAO-07-117SP (Washington, D.C.: December 2006). In January 2007 and 2008, we issued updates to this guide for fiscal years 2006 and 2007, GAO-07-341SP (Washington, D.C.: January 2007) and GAO-08-410SP (Washington, D.C.: January 2008).

Financial Statements of the United States Government for the Years Ended September 30, 2008, and September 30, 2007

Statements of Net Cost

These statements present the net cost of fiscal years 2008 and 2007 Government[1] operations, including the operations related to earmarked funds (funds financed by specifically identified revenues, often supplemented by other financing sources, which remain available over time). The Government's fiscal year begins October 1 and ends September 30. Costs are categorized on the Statement of Net Cost by significant entity. Costs and earned revenues are generally presented by department on an accrual basis, while the budget presents costs and revenues by obligations and outlays, generally on a cash basis. In the Statements of Net Cost, the costs and earned revenues are divided between the corresponding departments and entities mentioned above, providing greater accountability by showing the relationship of the agencies' net cost to the Governmentwide net cost. The focus of the budget of the United States is by agency. Budgets are prepared, defended, and monitored by agency. In reporting by agency, we are assisting the external users in assessing the budget integrity, operating performance, stewardship, and systems and control of the Government.

These statements contain the following three components:

- Gross cost—is the full cost of all the departments and entities. These costs are assigned on a cause-and-effect basis, or reasonably allocated to the corresponding departments and entities.
- Earned revenue—is exchange revenue resulting from the Government providing goods and services to the public at a price.
- Net cost—is computed by subtracting earned revenue from gross cost.

Net cost for Governmentwide reporting purposes includes the General Services Administration (GSA) and the Office of Personnel Management (OPM) agency allocations, and is net of intragovernmental eliminations. For this reason, individual agency net cost amounts will not agree with the agency's financial statements. Because of their specific functions, most of the costs originally associated with GSA and OPM have been allocated to the costs of their user agencies for Governmentwide reporting purposes. The remaining costs for GSA and OPM on the Statements of Net Cost are the administrative operating costs, the expenses from prior and past costs from health and pension plan amendments, and the actuarial gains and losses for these agencies. The interest on securities issued by the Department of the Treasury (Treasury) and held by the public is reported on Treasury's financial statements, but because of its importance, and the dollar amounts, it is reported separately in these statements.

Statements of Operations and Changes in Net Position

These statements report the results of Government operations which include the results of earmarked fund operations. They include non-exchange revenues that are generated principally by the Government's sovereign power to tax, levy duties, and assess fines and penalties. These statements also cover the cost of Government operations, net of revenue earned from the sale of goods and services to the public (exchange revenue). They further include certain adjustments and unreconciled transactions that affect the net position.

[1] For purposes of this document, "Government" refers to the United States Government.

Revenue

Individual income tax and tax withholdings include Federal Insurance Contributions Act (FICA)/Self-Employment Contributions Act (SECA) taxes and other taxes including payroll taxes. These taxes are characterized as non-exchange revenue.

Excise taxes consist of taxes collected for various items, such as airline tickets, gasoline products, distilled spirits and imported liquor, tobacco, firearms, and others. These are also characterized as non-exchange revenue.

Miscellaneous earned revenues consist of earned revenues received from the public with virtually no associated cost. Therefore, unlike other earned revenues on the Statement of Net Cost, miscellaneous earned revenues are not subtracted from gross cost to derive net cost. It also includes rents and royalties on the Outer Continental Shelf Lands resulting from the leasing and development of mineral resources on public lands.

Earmarked revenues are required by statute to be used for designated activities, benefits or purposes and must be accounted for separately from the rest of the Government's non-earmarked revenues. Refer to Note 21—Earmarked Funds for detailed information.

Intragovernmental interest represents interest earned from the investment of surplus earmarked revenues, which finance the deficit spending of non-earmarked operations. These investments are recorded as intragovernmental debt holdings and are included in Note 11, in the table titled Intragovernmental Debt Holdings: Federal Debt Securities Held as Investments by Government Accounts. These interest payments and the associated investments are eliminated in the consolidation process.

Net Cost of Government Operations

The net cost of Government operations (which is gross cost less earned revenue) flows through from the Statements of Net Cost. The net cost associated with earmarked activities is separately reported.

Intragovernmental Transfers

Intragovernmental transfers reflect amounts required by statute to be transferred from the General Fund of the Treasury to earmarked funds (An example of which is the annual transfer to the Department of Health and Human Services'(HHS) Supplementary Medical Insurance Trust Fund (Medicare Parts B and D) which receives sufficient funding from the General Fund to equal the annual costs incurred by these Medicare programs). Additionally, this line item includes contributions to earmarked funds made by Federal agencies on behalf of their employees, beneficiaries, or others.

Unmatched Transactions and Balances

Unmatched transactions and balances are adjustments needed to bring the change in net position into balance due to unreconciled intragovernmental differences, agency reporting errors, and timing differences in the consolidated financial statements. Refer to Note 1—Summary of Significant Accounting Policies and the Supplemental Information—Unmatched Transactions and Balances for detailed information.

Net Position, Beginning of Period

The net position, beginning of period, reflects the net position reported on the prior year's balance sheet as of the end of that fiscal year. The net position for earmarked funds is shown separately.

Prior period adjustments are revisions to adjust the beginning net position and balances presented on the prior year financial statements. Refer to Note 1B—Basis of Accounting and Revenue Recognition, and Note 18—Prior Period Adjustments for detailed information.

Net Position, End of Period

The net position, end-of-period, amount reflects the net position as of the end of the fiscal year. The net position for earmarked funds is shown separately.

Reconciliations of Net Operating Cost and Unified Budget Deficit

These statements reconcile the results of operations (net operating cost) on the Statements of Operations and Changes in Net Position to the unified budget deficit in the President's budget. The premise of the reconciliation is that the accrual and budgetary accounting bases share transaction data.

Receipts and outlays in the President's budget are measured primarily on a cash basis and differ from the accrual basis of accounting used in the *Financial Report*. These statements begin with the net results of operations (net operating cost), where operating revenues are reported on a modified cash basis of accounting and the net cost of Government operations on an accrual basis of accounting and reports activities where the bases of accounting for the components of net operating cost and the unified budget deficit differed.

Components of Net Operating Cost Not Part of the Budget Deficit

This information includes the operating components, such as the changes in benefits payable for veterans, military and civilian employees, the environmental liabilities, and depreciation expense not included in the budget results.

Components of the Budget Deficit Not Part of Net Operating Cost

This information includes the budget components, such as capitalized fixed assets, changes in net inventory, and increases in other assets not included in the operating results. These items impact the balance sheet only and are not part of the operating results.

Statements of Changes in Cash Balance from Unified Budget and Other Activities

The primary purpose of these statements is to report how the annual unified budget deficit relates to the change in the Government's cash and other monetary assets and debt held by the public. It explains why the unified budget deficit normally would not result in an equivalent change in the Government's cash and other monetary assets.

These statements reconcile the unified budget deficit to the change in cash and other monetary assets during the fiscal year and explain how the budget deficits (fiscal years 2008 and 2007) were financed. A budget deficit is the result of outlays (expenditures) exceeding receipts (revenue) during a particular fiscal year.

The budget deficit is typically financed through borrowings from the public. Other transactions also require cash disbursements and are not part of the repayments of the debt. These other transactions, such as the payment of interest on debt held by the public, contributed to the use of cash. These statements show the differences between accrual and cash budgetary basis, mainly because of timing differences in the financial statements.

Balance Sheets

The balance sheets show the Government's assets, liabilities, and net position. When combined with stewardship information, this information presents a more comprehensive understanding of the Government's financial position. The net position for earmarked funds is shown separately.

Assets

Assets included on the balance sheets are resources of the Government that remain available to meet future needs. The most significant assets that are reported on the balance sheets are property, plant, and equipment; cash and other monetary assets; inventories; and loans receivable. There are, however, other significant resources available to the Government that extend beyond the assets presented in these financial statements. Those resources include stewardship assets, including natural resources, and the Government's sovereign powers to tax, regulate commerce, set monetary policy and the power to print additional currency.

Liabilities and Net Position

Liabilities are obligations of the Government resulting from prior actions that will require financial resources. The most significant liabilities reported on the balance sheets are Federal debt securities held by the public and accrued interest and Federal employee and veteran benefits payable. Liabilities also include environmental and disposal liabilities and social insurance benefits due and payable as of the reporting date.

As with reported assets, the Government's responsibilities, policy commitments, and contingencies are much broader than these reported balance sheet liabilities. They include the social insurance programs in the Statements of Social Insurance and are disclosed in the Supplemental Information—Social Insurance section and a wide range of other programs under which the Government provides benefits and services to the people of this Nation, as well as certain future loss contingencies.

The magnitude and complexity of social insurance programs, coupled with the extreme sensitivity of projections relating to the many assumptions of the programs, produce a wide range of possible results. Note 23—Social Insurance describes the social insurance programs, reports long-range estimates that can be used to assess the financial condition of the programs, and explains some of the factors that impact the various programs. Using this information, readers can apply their own judgment as to the condition and sustainability of the individual programs.

Each of the social insurance programs has an associated trust fund to account for its activity. The collection of earmarked taxes and other earmarked revenue is credited to the corresponding trust fund that will use these funds to meet a particular Government purpose. If the collections from taxes and other sources exceed the payments to the beneficiaries, the excess revenue is invested in Treasury securities or "loaned" to the Treasury's General Fund; therefore, the trust fund balances do not represent cash. An explanation of the trust funds for social insurance and many of the other large trust funds is included in Note 21—Earmarked Funds. That note also contains information about trust fund receipts, disbursements, and assets.

The Government has entered into contractual commitments requiring the future use of financial resources and has unresolved contingencies where existing conditions, situations, or circumstances create uncertainty about future losses. Commitments, as well as contingencies that do not meet the criteria for recognition as liabilities on the balance sheets, but for which there is at least a reasonable possibility that losses have been incurred, are disclosed in Note 19—Contingencies and Note 20—Commitments.

Because of its sovereign power to tax and borrow, and the country's wide economic base, the Government has unique access to financial resources through generating tax revenues and issuing Federal debt securities. This provides the Government with the ability to meet present obligations and those that are anticipated from future operations and are not reflected in net position.

Statements of Social Insurance

The Statements of Social Insurance provide estimates of the status of the most significant social insurance programs: Social Security, Medicare, Railroad Retirement, and Black Lung social insurance programs, which are administered by the Social Security Administration, HHS, the Railroad Retirement Board (RRB), and the Department of Labor, respectively. The estimates are actuarial present values[2] of the projections and are based on the economic and demographic assumptions representing the trustees' best estimates as set forth in the relevant Social Security and Medicare trustees' reports and in the relevant agency performance and accountability reports for the RRB and the Department of Labor (Black Lung).

[2] Present values recognize that a dollar paid or collected in the future is worth less than a dollar today, because a dollar today could be invested and earn interest. To calculate a present value, future amounts are thus reduced using an assumed interest rate, and those reduced amounts are summed.

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United States Government
Statements of Net Cost
for the Years Ended September 30, 2008, and September 30, 2007

(In billions of dollars)	Gross Cost	Earned Revenue	Net Cost	Gross Cost	Earned Revenue	Net Cost
		2008			2007	
Department of Defense	767.6	26.8	740.8	689.6	25.1	664.5
Department of Health and Human Services	769.1	56.4	712.7	718.6	51.8	666.8
Social Security Administration	663.9	0.3	663.6	626.4	0.3	626.1
Department of Veterans Affairs	434.6	4.2	430.4	63.1	3.7	59.4
Interest on Treasury Securities held by the public	241.6	-	241.6	238.9	-	238.9
Department of the Treasury	197.0	12.4	184.6	86.9	6.3	80.6
Department of Agriculture	109.3	9.8	99.5	98.6	12.1	86.5
Department of Transportation	71.5	0.8	70.7	66.2	0.5	65.7
Department of Education	66.9	5.0	61.9	66.3	4.5	61.8
Department of Labor	60.6	-	60.6	50.1	-	50.1
Department of Housing and Urban Development	60.6	0.8	59.8	54.0	0.9	53.1
Department of Homeland Security	60.0	7.9	52.1	51.1	7.1	44.0
Department of Energy	35.8	4.2	31.6	67.5	4.3	63.2
Department of Justice	31.7	1.1	30.6	28.8	1.0	27.8
Office of Personnel Management	39.5	16.0	23.5	36.2	15.5	20.7
Federal Deposit Insurance Corporation	24.3	1.7	22.6	1.7	0.9	0.8
Department of the Interior	23.4	2.1	21.3	18.6	2.0	16.6
National Aeronautics and Space Administration	20.4	0.2	20.2	16.3	0.1	16.2
Department of State	22.1	2.6	19.5	18.4	3.4	15.0
Railroad Retirement Board	20.7	4.2	16.5	15.7	10.3	5.4
Department of Commerce	11.9	2.0	9.9	9.6	1.9	7.7
Environmental Protection Agency	10.1	0.5	9.6	10.0	0.4	9.6
Agency for International Development	9.1	(0.1)	9.2	9.7	0.3	9.4
Federal Communications Commission	8.5	0.4	8.1	7.9	0.4	7.5
National Science Foundation	6.0	-	6.0	5.7	-	5.7
Small Business Administration	1.9	0.4	1.5	1.3	0.4	0.9
Smithsonian Institution	0.9	-	0.9	0.7	-	0.7
General Services Administration	1.0	0.5	0.5	0.6	0.5	0.1
U.S. Nuclear Regulatory Commission	1.2	0.8	0.4	1.0	0.6	0.4
National Credit Union Administration	0.5	0.1	0.4	0.3	0.1	0.2
Securities and Exchange Commission	1.1	1.0	0.1	1.0	1.5	(0.5)
Tennessee Valley Authority	10.2	10.1	0.1	10.9	10.4	0.5
Farm Credit System Insurance Corporation	-	0.2	(0.2)	-	0.1	(0.1)
Export-Import Bank of the United States	0.4	0.7	(0.3)	0.5	0.9	(0.4)
Pension Benefit Guaranty Corporation	2.3	3.5	(1.2)	1.5	6.1	(4.6)
U.S. Postal Service	60.0	73.7	(13.7)	60.1	73.7	(13.6)
All other entities	45.9	0.6	45.3	23.5	0.7	22.8
Total	3,891.6	250.9	3,640.7	3,157.3	247.8	2,909.5

The accompanying notes are an integral part of these financial statements.

United States Government
Statements of Operations and Changes in Net Position for the Years Ended September 30, 2008, and September 30, 2007 (Restated-See Note 21)

(In billions of dollars)	Non-Earmarked Funds	Earmarked Funds	Consolidated	Non-Earmarked Funds	Earmarked Funds	Consolidated
		2008			2007 (Restated)	
Revenue:						
Individual income tax and tax withholdings	1,210.0	868.4	2,078.4	1,164.4	835.4	1,999.8
Corporation income taxes	299.7		299.7	367.2		367.2
Unemployment taxes		39.4	39.4		39.3	39.3
Excise taxes	15.3	51.8	67.1	13.9	53.6	67.5
Estate and gift taxes	28.8		28.8	26.0		26.0
Customs duties	27.3		27.3	18.2		18.2
Other taxes and receipts	50.7	34.3	85.0	44.4	35.2	79.6
Miscellaneous earned revenues	29.9	5.8	35.7	25.3	4.4	29.7
Intragovernmental interest		201.0	201.0		192.7	192.7
Total revenue	1,661.7	1,200.7	2,862.4	1,659.4	1,160.6	2,820.0
Eliminations			(201.0)			(192.7)
Consolidated revenue			2,661.4			2,627.3
Net Cost:						
Net cost	2,186.4	1,454.3	3,640.7	1,653.1	1,256.4	2,909.5
Intragovernmental interest	201.0		201.0	192.7		192.7
Total net cost	2,387.4	1,454.3	3,841.7	1,845.8	1,256.4	3,102.2
Eliminations			(201.0)			(192.7)
Consolidated net cost			3,640.7			2,909.5
Intragovernmental transfers	(338.0)	338.0		(290.6)	290.6	
Unmatched transactions and balances (Note 1)	(29.8)		(29.8)	6.7		6.7
Net operating (cost)/revenue	(1,093.5)	84.4	(1,009.1)	(470.3)	194.8	(275.5)
Net position, beginning of period	(9,826.0)	620.2	(9,205.8)	(9,340.7)	424.3	(8,916.4)
Prior period adjustments – changes in accounting principles (Note 18)	11.4	-	11.4	(15.0)	1.1	(13.9)
Net operating (cost)/revenue	(1,093.5)	84.4	(1,009.1)	(470.3)	194.8	(275.5)
Net position, end of period	(10,908.1)	704.6	(10,203.5)	(9,826.0)	620.2	(9,205.8)

The accompanying notes are an integral part of these financial statements.

United States Government
Reconciliations of Net Operating Cost and Unified Budget Deficit
for the Years Ended September 30, 2008, and September 30, 2007

(In billions of dollars)	2008	2007
Net Operating Cost	(1,009.1)	(275.5)
Components of Net Operating Cost Not Part of the Budget Deficit:		
Increase in Liability for Military Employee Benefits (Note 12):		
Increase in military pension liabilities	125.3	61.7
(Decrease) in military health liabilities	(15.3)	(1.3)
(Decrease) in other military benefits	(0.1)	(0.1)
Increase in liability for military employee benefits	109.9	60.3
Increase (Decrease) in liability for veteran's compensation (Note 12):		
Increase (Decrease) in liabilities for veterans	287.9	(26.8)
Increase in liabilities for survivors	50.2	0.8
Increase (Decrease) in liabilities for burial benefits	0.9	(0.1)
Increase (Decrease) in liability for veteran's compensation	339.0	(26.1)
Increase in liabilities for civilian employee benefits (Note 12):		
Increase in civilian pension liabilities	68.5	37.3
Increase in civilian health liabilities	30.2	16.4
Increase in other civilian benefits	2.2	2.2
Increase in liabilities for civilian employee benefits	100.9	55.9
Increase in environmental and disposal liabilities (Note 13):		
Increase in Energy's environmental and disposal liabilities	2.4	33.3
(Decrease) Increase in all others' environmental and disposal liabilities	(1.6)	3.5
Increase in environmental and disposal liabilities	0.8	36.8
Depreciation expense	54.8	45.3
Property, plant, and equipment disposals and revaluations	5.0	10.9
Increase in benefits due and payable	10.7	4.4
Increase (Decrease) in insurance program liabilities	5.1	(0.1)
Increase in other liabilities	41.6	21.8
Seigniorage and sale of gold	(0.7)	(0.8)
Increase in accounts payable	7.1	7.8
(Increase) in net accounts and taxes receivable	(5.2)	(19.0)
(Increase) in Investments in Government Sponsored Enterprises	(7.0)	-
Increase in Keepwell Payable	13.8	-
Components of the budget deficit that are not part of net operating cost:		
Capitalized Fixed Assets		
Department of Defense	(71.6)	(29.1)
All Other Agencies	(34.8)	(29.7)
Total Capitalized Fixed Assets	(106.4)	(58.8)
(Increase) Decrease in net inventory	(12.5)	4.2
Decrease (Increase) in Securities and Investments	18.2	(12.9)
(Increase) in other assets	(14.5)	(10.0)
Principal repayments of precredit reform loans	5.1	8.5
All Other Reconciling items	(11.4)	(15.5)
Unified budget deficit	(454.8)	(162.8)

The accompanying notes are an integral part of these financial statements.

United States Government
Statements of Changes in Cash Balance from Unified Budget and Other Activities for the Years Ended September 30, 2008, and September 30, 2007

(In billions of dollars)	2008		2007	
Unified budget deficit		(454.8)		(162.8)
Adjustments for noncash outlays included in the budget:				
Interest accrued by Treasury on debt held by the public	209.0		189.4	
Subsidy expense (Note 4)	(3.0)		(9.3)	
Subtotal		206.0		180.1
Items affecting the cash balance not included in the Budget:				
Net Transactions from financing activity:				
Borrowings from the public	5,615.8		4,547.3	
Repayment of debt held by the public	(4,853.1)		(4,340.4)	
Agency securities	-		(0.4)	
Subtotal		762.7		206.5
Net transactions from monetary and other activity:				
Interest paid by Treasury on debt held by the public	(213.3)		(186.1)	
Other	(4.1)		(7.6)	
Subtotal		(217.4)		(193.7)
Cash and other monetary assets: (Note 2):				
Increase in cash and other monetary assets		296.5		30.1
Balance beginning of period		128.0		97.9
Balance end of period		424.5		128.0

The accompanying notes are an integral part of these financial statements.

United States Government
Balance Sheets
as of September 30, 2008, and September 30, 2007
(Restated-See Note 21)

(In billions of dollars)	2008	2007 (Restated)
Assets:		
Cash and other monetary assets (Note 2)	424.5	128.0
Accounts and taxes receivable, net (Note 3)	93.0	87.8
Loans receivable, net (Note 4)	263.4	231.9
Inventories and related property, net (Note 5)	289.6	277.1
Property, plant, and equipment, net (Note 6)	737.7	691.1
Securities and investments (Note 7)	79.6	99.8
Investments in Government sponsored enterprises (Note 8)	7.0	-
Other assets (Note 9)	79.9	65.4
Total assets	1,974.7	1,581.1
Stewardship Land and Heritage Assets (Note 24)		
Liabilities:		
Accounts payable (Note 10)	73.3	66.2
Federal debt securities held by the public and accrued interest (Note 11)	5,836.2	5,077.7
Federal employee and veteran benefits payable (Note 12)	5,318.9	4,769.1
Environmental and disposal liabilities (Note 13)	342.8	342.0
Benefits due and payable (Note 14)	144.4	133.7
Insurance program liabilities (Note 15)	77.8	72.7
Loan guarantee liabilities (Note 4)	72.9	69.1
Keepwell payable (Note 8)	13.8	-
Other liabilities (Note 16)	298.1	256.4
Total liabilities	12,178.2	10,786.9
Contingencies (Note 19) and Commitments (Note 20)		
Net position:		
Earmarked funds (Note 21) (Restated)	704.6	620.2
Non-earmarked funds (Restated)	(10,908.1)	(9,826.0)
Total net position	(10,203.5)	(9,205.8)
Total liabilities and net position	1,974.7	1,581.1

The accompanying notes are an integral part of these financial statements.

United States Government
Statements of Social Insurance (Note 23)
Present Value of Long-Range (75 Years, except Black Lung) Actuarial Projections

(In billions of dollars)	2008	2007	2006	***UNAUDITED*** 2005	2004
Federal Old-Age, Survivors and Disability Insurance (Social Security): [14]					
Revenue (Contributions and Earmarked Taxes) from:					
Participants who have attained eligibility age (62 and over)	542	477	533	464	411
Participants who have not attained eligibility age	18,249	17,515	16,568	15,290	14,388
Future participants	17,566	16,121	15,006	13,696	12,900
All current and future participants	36,357	34,113	32,107	29,450	27,699
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (62 and over)	(6,958)	(6,329)	(5,866)	(5,395)	(4,933)
Participants who have not attained eligibility age	(29,021)	(27,928)	(26,211)	(23,942)	(22,418)
Future participants	(6,933)	(6,619)	(6,480)	(5,816)	(5,578)
All current and future participants	(42,911)	(40,876)	(38,557)	(35,154)	(32,928)
Present value of future expenditures in excess of future revenue	(6,555) [1]	(6,763) [2]	(6,449) [3]	(5,704) [4]	(5,229) [5]
Federal Hospital Insurance (Medicare Part A): [14]					
Revenue (Contributions and Earmarked Taxes) from:					
Participants who have attained eligibility age (65 and over)	202	178	192	162	148
Participants who have not attained eligibility age	6,320	5,975	5,685	5,064	4,820
Future participants	5,361	4,870	4,767	4,209	4,009
All current and future participants	11,883	11,023	10,644	9,435	8,976
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (65 and over)	(2,747)	(2,558)	(2,397)	(2,179)	(2,168)
Participants who have not attained eligibility age	(17,365)	(15,639)	(15,633)	(12,668)	(12,054)
Future participants	(4,506)	(5,118)	(3,904)	(3,417)	(3,246)
All current and future participants	(24,619)	(23,315)	(21,934)	(18,264)	(17,468)
Present value of future expenditures in excess of future revenue	(12,736) [1]	(12,292) [2]	(11,290) [3]	(8,829) [4]	(8,492) [5]
Federal Supplementary Medical Insurance (Medicare Part B): [14]					
Revenue (Premiums) from:					
Participants who have attained eligibility age (65 and over)	461	433	409	363	332
Participants who have not attained eligibility age	3,859	3,184	3,167	2,900	2,665
Future participants	1,158	1,172	906	924	891
All current and future participants	5,478	4,789	4,481	4,187	3,889
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (65 and over)	(1,986)	(1,834)	(1,773)	(1,622)	(1,475)
Participants who have not attained eligibility age	(14,949)	(12,130)	(12,433)	(11,541)	(10,577)
Future participants	(4,262)	(4,257)	(3,407)	(3,408)	(3,277)
All current and future participants	(21,197)	(18,221)	(17,613)	(16,571)	(15,329)
Present value of future expenditures in excess of future revenue [6]	(15,719) [1]	(13,432) [2]	(13,131) [3]	(12,384) [4]	(11,440) [5]

Totals may not equal the sum of components due to rounding.

The accompanying notes are an integral part of these financial statements.

United States Government
Statements of Social Insurance (Note 23), continued
Present Value of Long-Range (75 Years, except Black Lung) Actuarial Projections

(In billions of dollars)	2008	2007	2006	***UNAUDITED*** 2005	2004
Federal Supplementary Medical Insurance (Medicare Part D): [14]					
Revenue (Premiums and State Transfers) from:					
Participants who have attained eligibility age (65 and over)	123	167	173	185	176
Participants who have not attained eligibility age	1,380	1,627	1,700	1,790	1,857
Future participants	604	611	492	572	618
All current and future participants	2,107	2,405	2,366	2,547	2,651
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (65 and over)	(581)	(794)	(792)	(880)	(773)
Participants who have not attained eligibility age	(6,527)	(7,273)	(7,338)	(7,913)	(7,566)
Future participants	(2,856)	(2,699)	(2,121)	(2,440)	(2,431)
All current and future participants	(9,964)	(10,766)	(10,250)	(11,233)	(10,770)
Present value of future expenditures in excess of future revenue [6]	(7,857) [1]	(8,361) [2]	(7,884) [3]	(8,686) [4]	(8,119) [5]
Railroad Retirement:					
Revenue (Contributions and Earmarked Taxes) from:					
Participants who have attained eligibility	5	5	5	4	4
Participants who have not attained eligibility	43	41	40	37	37
Future participants	54	54	56	41	39
All current and future participants	102	100	100	82	80
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility	(97)	(93)	(92)	(84)	(81)
Participants who have not attained eligibility	(88)	(86)	(84)	(73)	(72)
Future participants	(26)	(26)	(25)	(16)	(14)
All current and future participants	(212)	(205)	(201)	(173)	(167)
Present value of future expenditures in excess of future revenue [7]	(109) [1]	(105) [2]	(101) [3]	(91) [4]	(87) [5]
Black Lung (Part C):					
Present value of future revenue in excess of future expenditures [8]	5 [9]	5 [10]	4 [11]	5 [12]	4 [13]
Total present value of future expenditures in excess of future revenue	(42,970)	(40,948)	(38,851)	(35,689)	(33,363)

Totals may not equal the sum of components due to rounding.

The accompanying notes are an integral part of these financial statements.

United States Government
Statements of Social Insurance (Note 23), continued
Present Value of Long-Range (75 Years, except Black Lung) Actuarial Projections

				UNAUDITED	
(In billions of dollars)	2008	2007	2006	2005	2004
Social Insurance Summary: [14]					
Participants who have attained eligibility age:					
Revenue (e.g., Contributions and earmarked taxes)	1,333	1,260	1,312	1,178	1,071
Expenditures for scheduled future benefits	(12,369)	(11,608)	(10,920)	(10,160)	(9,430)
Present value of future expenditures in excess of future revenue	(11,036)	(10,348)	(9,608)	(8,982)	(8,359)
Participants who have not attained eligibility age:					
Revenue (e.g., Contributions and earmarked taxes)	29,851	28,342	27,160	25,081	23,767
Expenditures for scheduled future benefits	(67,950)	(63,056)	(61,696)	(56,138)	(52,686)
Present value of future expenditures in excess of future revenue	(38,099)	(34,714)	(34,536)	(31,057)	(28,919)
Closed group – Total present value of future expenditures in excess of future revenue	(49,135)	(45,062)	(44,145)	(40,039)	(37,278)
Future participants:					
Revenue (e.g., Contributions and earmarked taxes)	24,743	22,828	21,227	19,442	18,457
Expenditures for scheduled future benefits	(18,578)	(18,714)	(15,933)	(15,092)	(14,542)
Present value of future revenue in excess of future expenditures	6,165	4,114	5,294	4,350	3,915
Open group – Total present value of future expenditures in excess of future revenue	(42,970)	(40,948)	(38,851)	(35,689)	(33,363)

[1] The projection period is 1/1/2008 - 12/31/2082 and the valuation date is 1/1/2008.
[2] The projection period is 1/1/2007 - 12/31/2081 and the valuation date is 1/1/2007.
[3] The projection period is 1/1/2006 - 12/31/2080 and the valuation date is 1/1/2006.
[4] The projection period is 1/1/2005 - 12/31/2079 and the valuation date is 1/1/2005.
[5] The projection period is 1/1/2004 - 12/31/2078 and the valuation date is 1/1/2004.
[6] These amounts represent the present value of the future transfers from the General Fund of the Treasury to the Supplementary Medical Insurance Trust Fund. These future intragovernmental transfers are included as income in both HHS' and the Centers for Medicare & Medicaid Services' Financial Reports but are not income from the Governmentwide perspective of this report.
[7] These amounts approximate the present value of the future financial interchange and the future transfers from the General Fund of the Treasury to the Social Security Equivalent Benefit Account (see discussion of Railroad Retirement Program in the required supplemental information section of this report). They are included as income in the Railroad Retirement Financial Report but are not income from the Governmentwide perspective of this report.
[8] Does not include interest expense accruing on the outstanding debt.
[9] The projection period is 9/30/2008 - 9/30/2040 and the valuation date is 9/30/2008.
[10] The projection period is 9/30/2007 - 9/30/2040 and the valuation date is 9/30/2007.
[11] The projection period is 9/30/2006 - 9/30/2040 and the valuation date is 9/30/2006.
[12] The projection period is 9/30/2005 - 9/30/2040 and the valuation date is 9/30/2005.
[13] The projection period is 9/30/2004 - 9/30/2040 and the valuation date is 9/30/2004.
[14] Participants for the Social Security and Medicare programs are assumed to be the "closed group" of individuals who are at least age 15 at the start of the projection period, and are participating as either taxpayers, beneficiaries, or both, except for the 2007 Medicare programs for which current participants are assumed to be at least 18 instead of 15 years of age.

Totals may not equal the sum of components due to rounding.

The accompanying notes are an integral part of these financial statements.

United States Government Notes to the Financial Statements for the Years Ended September 30, 2008, and September 30, 2007

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

This *Financial Report* includes the financial status and activities of the executive branch, the legislative branch (the U.S. Senate and the U.S. House of Representatives report on a cash basis), and the judicial branch (which also reports on a cash basis) of the Government. The judicial branch reports on a limited basis primarily related to budget activity because it is not required by law to submit financial statement information to the Department of the Treasury (Treasury). The Appendix section of this report contains a list of significant Government entities included and excluded in the *Financial Report*. Certain entities are excluded from the *Financial Report* because they are Government sponsored enterprises (GSE), such as the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac), or their activities are not included in the Federal budget, such as the Thrift Savings Fund and the Board of Governors of the Federal Reserve System.

In September 2008, the Government began a number of emergency economic measures relating to the economy which involved various financing programs. Key initiatives effective for fiscal year 2008 involved programs concerning two GSEs, provision of a credit facility for GSE and Federal Home Loan Banks, purchase of Mortgage Backed Securities (MBS), and setup of a Money Market Insurance Program (see Notes 8 and 25).

Material intragovernmental transactions are eliminated in consolidation, except as described below in this note and in the Supplemental Information—Unmatched Transactions and Balances. The financial reporting period ends September 30 and is the same as used for the annual budget.

B. Basis of Accounting and Revenue Recognition

These financial statements were prepared using U.S. Generally Accepted Accounting Principles (GAAP), primarily based on Statements of Federal Financial Accounting Standards (SFFAS). Under these principles:

- Expenses are generally recognized when incurred.
- Nonexchange revenues, including taxes, duties, fines, and penalties, are recognized when collected and adjusted to the change in net measurable and legally collectable amounts receivable. Related refunds and other offsets, including those that are measurable and legally payable, are netted against nonexchange revenue.
- Exchange (earned) revenues are recognized when the Government provides goods and services to the public for a price. Exchange revenues include user charges such as admission to Federal parks and premiums for certain Federal insurance.

The basis of accounting used for budgetary purposes, which is primarily on a cash and obligation basis and follows budgetary concepts and policies, differs from the basis of accounting used for the financial statements which follow U.S. GAAP. See the Reconciliations of Net Operating Cost and Unified Budget Deficit in the Financial Statements section.

C. Direct Loans and Loan Guarantees

Direct loans obligated and loan guarantees committed after fiscal year 1991 are reported based on the present value of the net cashflows estimated over the life of the loan or guarantee. The difference between the outstanding principal of the direct loans and the present value of their net cash inflows is recognized as a subsidy cost allowance. The present value of estimated net cash outflows of the loan guarantees is recognized as a liability for loan guarantees.

The subsidy expense for direct or guaranteed loans disbursed during a year is the present value of estimated net cash outflows for those loans or guarantees. A subsidy expense also is recognized for modifications made during the year to loans and guarantees outstanding and for reestimates made as of the end of the year to the subsidy allowances or loan guarantee liability for loans and guarantees outstanding.

Direct loans obligated and loan guarantees committed before fiscal year 1992 are valued under two different methodologies within the Government: the allowance-for-loss method and the present-value method. Under the allowance-for-loss method, the outstanding principal of direct loans is reduced by an allowance for uncollectible amounts; the liability for loan guarantees is the amount the agency estimates would more likely than not require future cash outflow to pay default claims.

Under the present-value method, the outstanding principal of direct loans is reduced by an allowance equal to the difference between the outstanding principal and the present value of the expected net cashflows. The liability for loan guarantees is the present value of expected net cash outflows due to the loan guarantees.

D. Accounts and Taxes Receivable

Accounts receivable represent claims to cash or other assets from entities outside the Government that arise from the sale of goods or services, duties, fines, certain license fees, recoveries, or other provisions of the law. Accounts receivable are reported net of an allowance for uncollectible accounts. An allowance for estimated losses due to uncollectible amounts is established when it is more likely than not the receivables will not be totally collected. The allowance method varies among the agencies in the Government and is usually based on past collection experience and is re-estimated periodically as needed. Methods include statistical sampling of receivables, specific identification and intensive analysis of each case, aging methodologies, and percentage of total receivables based on historical collection.

Taxes receivable consist primarily of uncollected tax assessments, penalties, and interest when taxpayers have agreed the amounts are owed or a court has determined the assessments are owed. The balance sheets do not include unpaid assessments when neither taxpayers nor a court have agreed that the amounts are owed (compliance assessments) or the Government does not expect further collections due to factors such as the taxpayer’s death, bankruptcy, or insolvency (writeoffs). Taxes receivable are reported net of an allowance for the estimated portion deemed to be uncollectible. The allowance for doubtful accounts is based on projections of collectibility from a statistical sample of unpaid tax assessments.

E. Inventories and Related Property

Inventories within the Government are valued using historical cost, net realizable value, and latest acquisition cost (see Note 5—Inventories and Related Property, Net). Historical cost methods include first-in-first-out, weighted average, and moving average. Estimated repair costs reduce the value of inventory held for repair. Excess, obsolete, and unserviceable inventories are valued at estimated net realizable value. When latest acquisition cost is used to value inventory held for sale, it is adjusted for holding gains and losses in order to approximate historical cost.

Related property includes operating materials and supplies, stockpile materials, commodities, seized and monetary instruments, and forfeited property. Operating materials and supplies are valued at historical cost, latest acquisition cost, and standard price using the purchase and consumption method of accounting. Operating materials and supplies that are valued at latest acquisition cost and standard pricing are not adjusted for holding gains and losses.

F. Property, Plant, and Equipment

Property, plant, and equipment consists of tangible assets including equipment, buildings, construction in progress, internal use software, and other assets used to provide goods and services.

Property, plant, and equipment used in Government operations are carried at acquisition cost, with the exception of Department of Defense (DOD) military equipment (e.g., ships, aircraft, combat vehicles, and weapons). DOD uses an estimation methodology for military equipment based on internal DOD records to calculate a value for military equipment. DOD identified the universe of military equipment by accumulating information relating to program funding and associated military equipment, equipment useful life, and program acquisitions and disposals to create a baseline. The equipment baseline is updated using expenditure information and information related to acquisition and logistics to identify acquisitions and disposals.

All property, plant, and equipment is capitalized if the acquisition costs (or estimated acquisition cost for DOD) are in excess of capitalization thresholds that vary considerably between the Federal entities. Depreciation and amortization expense applies to property, plant, and equipment reported on the balance sheets except for land, unlimited duration land rights and construction in progress. Depreciation and amortization are recognized using the straight-line method over the estimated useful lives of the assets. All property, plant, and equipment are assigned useful lives depending on their category and vary considerably between the Federal entities. The cost of acquisition, betterment, or reconstruction of all multi-use heritage assets is capitalized as general property, plant, and equipment and is depreciated. Construction in progress is used for the accumulation of the cost of construction or major renovation of fixed assets during the construction period. The assets are transferred out of construction in progress when the project is substantially completed. Internal use software includes purchased commercial off-the-shelf software, contractor-developed software, and software internally developed.

G. Federal Employee and Veteran Benefits Payable

Generally, Federal employee and veteran benefits payable are recorded during the time employee services are rendered. The related liabilities for defined benefit pension plans, veterans' compensation and burial benefits, post-retirement health benefits, life insurance benefits, and Federal Employee and Compensation Act benefits are recorded at estimated present value of future benefits, less any estimated present value of future normal cost contributions. The estimated present value for veterans' pension benefits is disclosed but is not included in the Federal employee and veteran benefits payable line. These benefits are expensed when services are provided.

Normal cost is the portion of the actuarial present value of projected benefits allocated as an expense for employee services rendered in the current year. Actuarial gains and losses (and prior service cost, if any) are recognized immediately in the year they occur, without amortization.

H. Environmental and Disposal Liabilities

Environmental and disposal liabilities are recorded at the estimated current cost of removing, containing, treating, and/or disposing of radioactive waste, hazardous waste, chemical and nuclear weapons, and other environmental contaminations, assuming the use of current technology. Hazardous waste is a solid, liquid, or gaseous waste that, because of its quantity or concentration, presents a potential hazard to human health or the environment. Remediation consists of removal, decontamination, decommissioning, site restoration, site monitoring, closure and post-closure cost, treatment, and/or safe containment. Where technology does not exist to clean up radioactive or hazardous waste, only the estimable portion of the liability, typically monitoring and safe containment is recorded.

I. Insurance Program Liabilities

Insurance programs provide protection to individuals or entities against specified risks except for those specifically covered by Federal employee and veteran benefits. Insurance program funds are commonly held in revolving funds in the Government and losses sustained by participants are paid from these funds. Many of these programs receive appropriations to pay excess claims and/or have authority to borrow from the Treasury. The values of insurance program liabilities are particularly sensitive to changes in underlying estimates and assumptions, which are subject to change.

J. Deferred Maintenance

Deferred maintenance is maintenance that was not performed when it should have been or scheduled maintenance that was delayed or postponed. Maintenance is the act of keeping fixed assets in acceptable condition, including preventative maintenance, normal repairs, and other activities needed to preserve the assets, so they continue to provide acceptable services and achieve their expected life. Maintenance excludes activities aimed at expanding the capacity of assets or otherwise upgrading them to serve needs different from those originally intended. Deferred maintenance expenses are not accrued in the Statements of Net Cost or recognized as liabilities on the balance sheets. However, deferred maintenance information is disclosed in the Supplemental Information section of this report.

K. Contingent Liabilities

Liabilities for contingencies are recognized on the balance sheets when both:

- A past transaction or event has occurred, and
- A future outflow or other sacrifice of resources is probable and measurable.

The estimated contingent liability may be a specific amount or a range of amounts. If some amount within the range is a better estimate than any other amount within the range, then that amount is recognized. If no amount within the range is a better estimate than any other amount, then the minimum amount in the range is recognized.

Contingent liabilities that do not meet the above criteria for recognition, but for which there is at least a reasonable possibility that a loss may have been incurred, is disclosed in Note 19—Contingencies.

L. Commitments

In the normal course of business, the Government has a number of unfulfilled commitments that may require the use of its financial resources. Note 20—Commitments describes the components of the Government's actual commitments that need to be disclosed because of their nature and/or their amount. They include long-term leases, undelivered orders, and other commitments.

Discussion of treaties and other international agreements entered into by the United States Government are also included in the Commitments section.

M. Social Insurance

A liability for social insurance programs (Social Security, Medicare, Railroad Retirement, Black Lung, and Unemployment) is recognized for any unpaid amounts currently due as of the reporting date. No liability is recognized for future benefit payments not yet due. For further information, see the Supplemental Information—Social Insurance section, and Note 23—Social Insurance.

N. Related Party Transactions

Federal Reserve banks (FRBs) and private banks, which are not part of the reporting entity, serve as the Government's depositary and fiscal agents. They process Federal payments and deposits to Treasury's account and service Treasury securities. As of September 30, 2008, FRBs owned $221.3 billion, net of $255.3 billion in securities lent to dealers, for total holdings of $476.6 billion. As of September 30, 2007, the FRBs owned $774.5 billion, net of $5.1 billion in securities lent to dealers, for total holdings of $779.6 billion. These securities are held in the FRBs System Open Market Account (SOMA) for the purpose of conducting monetary policy. Additionally, under the Supplementary Financing Program (SFP), the Government had on deposit $300 billion with the Federal Reserve as of September 30, 2008, to support Federal Reserve initiatives (see Note 2). FRBs earnings that exceed statutory amounts of surplus established for FRBs are paid to the Government and are recognized as nonexchange revenue. Those earnings totaled $33.6 billion and $32.0 billion for the years ended September 30, 2008, and 2007, respectively. The primary source of these earnings is from interest earned on Treasury securities held by the FRBs. Also, as described in Note 16—Other Liabilities, the FRBs hold certificates and special drawing rights certificates. The FRBs also was a key player in actions taken in fiscal year 2008 to stabilize the housing and financial markets (see Note 8).

FRBs issue Federal Reserve notes, the circulating currency of the United States. Specific assets owned by FRBs, typically Treasury securities, collateralize these notes. Federal Reserve notes are backed by the full faith and credit of the Government.

The Government generally does not guarantee payment of the liabilities of Government-sponsored enterprises such as Fannie Mae, Freddie Mac, or the Federal Home Loan Banks, which are privately owned. Fannie Mae and Freddie Mac have been placed under conservatorship as of September 7, 2008, and the Government now guarantees, up to $200 billion, to provide additional capital to the extent that liabilities exceeds assets (see Note 8). These enterprises also are excluded from the reporting entity.

O. Unmatched Transactions and Balances

The reconciliation of the change in net position requires that the difference between ending and beginning net position equals the excess of revenues over net cost, plus or minus prior period adjustments.

The unmatched transactions and balances are needed to bring the change in net position into balance. The primary factors affecting this out of balance situation are:

- Unmatched intragovernmental transactions and balances between Federal agencies,
- General fund transactions, and
- Timing differences and errors in Federal agencies' reporting.

Refer to the Supplemental Information—Unmatched Transactions and Balances for detailed information.

P. Reclassifications and Restatements

Certain fiscal year 2007 amounts have been reclassified to conform to the fiscal year 2008 presentation. See Note 21 for Restatements.

Q. Use of Estimates

The Government has made certain estimates and assumptions relating to the reporting of assets, liabilities, revenues, expenses, and the disclosure of contingent liabilities that are used to prepare these financial statements. Actual results could differ from these estimates. Major items subject to estimates include loan receivables (including MBS); investments in non-Federal securities (including Freddie Mac and Fannie Mae); taxes receivables; depreciation; money market insurance liability; liability for liquidity commitment (Freddie Mac and Fannie Mae); imputed costs; actuarial liabilities; cost and earned revenue allocations; contingent legal liabilities; and credit reform subsidy costs.

The Government recognizes the sensitivity of credit reform modeling to slight changes in some model assumptions and uses continual review of model factors, statistical modeling, and annual re-estimates to reflect the most accurate cost of the credit programs to the U.S. Government. Two of the emergency economic programs that the Government implemented in the latter part of September 2008, the purchase program for MBS and the GSE credit facility, both operate under the provisions of credit reform and the use of estimates as dictated by the Federal Credit Reform Act. Further, the assumptions underlying the estimated future liquidity payments to the GSE are subject to a high level of market volatility, so that actual future payments may differ significantly from current estimates due to changing circumstances. The Troubled Asset Relief Program described further in Note 25 will also require the use of sophisticated estimates.

The Government used the following methodologies for valuation of the investment in GSE:

- **Common Stock Warrants:** The Black-Scholes Option Model (1973) was used to affirm that the value of the warrants is insensitive to the usual option input variables, including time to expiration and stock volatility, and the value per warrant share is nominally less than the trading price at September 30, 2008.
- **Senior Preferred Stock:** These shares were valued based on an interpolation of market prices during the five trading days prior to the announcement of the senior preferred stock purchase agreement for (i) Fannie Mae and Freddie Mac subordinated debt, as adjusted for the tax advantage of stock dividends compared with taxable interest, and (ii) Fannie Mae and Freddie Mac preferred stock.

Note 2. Cash and Other Monetary Assets

Cash and Other Monetary Assets as of September 30

(In billions of dollars)	2008	2007
Unrestricted cash:		
Cash held by Treasury for Governmentwide Operations	64.3	69.7
Other	6.5	6.4
Restricted cash:		
Cash held by Treasury for Governmentwide Operations	300.0	-
Other	14.0	13.5
Total cash	384.8	89.6
International monetary assets	14.3	13.9
Gold	11.0	11.0
Foreign currency	14.4	13.5
Total cash and other monetary assets	424.5	128.0

Unrestricted cash includes cash held by Treasury for Governmentwide operations (Operating Cash) and all other unrestricted cash held by the Federal agencies. Operating Cash represents balances from tax collections, other revenue, Federal debt receipts, and other various receipts net of cash outflows for budget outlays and other payments. Operating Cash includes balances invested with commercial depositaries in Treasury Tax and Loan Accounts (including funds invested through the Term Investment Option program and the Repo Pilot program). Treasury checks outstanding are netted against Operating Cash until they are cleared by the Federal Reserve System. Other unrestricted cash not included in Treasury's Operating Cash balance includes balances representing cash, cash equivalents, and other funds held by agencies, such as undeposited collections, deposits in transit, demand deposits, amounts held in trust, imprest funds, and amounts representing the balances of petty cash.

Restricted cash is restricted due to the imposition on cash deposits by law, regulation, or agreement. Restricted cash includes the SFP and cash held by the Foreign Military Sales programs. On September 18, 2008, Treasury began issuing specific cash management bills to fund the SFP. The SFP is a temporary program that deposits cash with the Federal Reserve to support Federal Reserve initiatives aimed at addressing the ongoing crisis in financial markets. As of September 30, 2008, there was a total of eight cash management bills outstanding related to SFP that totaled $300 billion. The issuing of these cash management bills leads to the large amount in the restricted cash balance as of September 30, 2008. The Foreign Military Sales program included $13.3 billion and $12.4 billion as of September 30, 2008, and 2007, respectively. This year, $12.4 billion was reclassified from unrestricted to restricted cash for this program. All cash held by depositary institutions is either insured (for balances up to $100,000 and temporarily increased to $250,000 per Note 25) by the Federal Deposit Insurance Corporation (FDIC) or collateralized by securities pledged by the depositary institution or through securities held under reverse repurchase agreements. See Note 25—Subsequent Events for a discussion on the change in insured limits.

International monetary assets include the U.S. reserve position in the International Monetary Fund (IMF) and U.S. holdings of Special Drawing Rights (SDRs).

The U.S. reserve position in the IMF reflects the reserve asset portion of the financial subscription that the United States has paid in as part of its participation in the IMF. The IMF promotes international monetary cooperation and a stable payment system to facilitate growth in the world economy. Its primary activities are surveillance of member economies, financial assistance as appropriate and technical assistance.

Only a portion of the U.S. financial subscriptions to the IMF is made in the form of reserve assets; the remainder is provided in the form of a letter of credit from the United States to the IMF. The balance available under the letter of credit totaled $53.0 billion and $53.2 billion as of September 30, 2008, and 2007, respectively. The U.S. reserve position in the IMF has a U.S. dollar equivalent of $4.8 billion and $4.5 billion as of September 30, 2008, and 2007, respectively.

SDRs are in international monetary reserves issued by the IMF. These interest-bearing assets can be obtained by IMF allocations, transactions with IMF member countries, interest earnings on SDR holdings, or U.S. reserve position in the IMF. SDR holdings are an asset of Treasury's Exchange Stabilization Fund (ESF), which held SDRs totaling $9.5 billion and $9.4 billion equivalent as of September 30, 2008, and 2007, respectively.

The IMF allocates SDRs to its members in proportion to each member's quota in the IMF. The SDR Act of 1968 authorized the Secretary of the Treasury to issue SDR Certificates (SDRCs) to the Federal Reserve in exchange for dollars. The amount of SDRCs outstanding cannot exceed the dollar value of SDR holdings. The Secretary of the Treasury determines when Treasury will issue or redeem SDRCs. SDRCs outstanding totaled $2.2 billion as of September 30, 2008, and 2007, and are included in Note 16—Other Liabilities.

As of September 30, 2008, and 2007, other liabilities included $7.6 billion of interest-bearing liability to the IMF for SDR allocations. The SDR allocation item represents the cumulative total of SDRs distributed by the IMF to the United States in allocations that occurred in 1970, 1971, 1972, 1979, 1980, and 1981.

Gold is valued at the statutory price of $42.2222 per fine troy ounce. The number of fine troy ounces was 261,498,900 as of September 30, 2008, and 2007. The market value of gold on the London Fixing was $885 and $743 per fine troy ounce as of September 30, 2008, and 2007, respectively. Gold totaling $11.0 billion as of September 30, 2008, and 2007, was pledged as collateral for gold certificates issued and authorized to the FRBs by the Secretary of the Treasury. Treasury may redeem the gold certificates at any time. The liabilities for the gold certificates issued are included in Note 16—Other Liabilities.

Foreign currency is translated into U.S. dollars at the exchange rate at fiscal yearend. The foreign currency is maintained by various U.S. Federal agencies and foreign banks.

Note 3. Accounts and Taxes Receivable, Net

Accounts and Taxes Receivable as of September 30

(In billions of dollars)	2008	2007
Accounts Receivable:		
Department of Agriculture	10.1	8.9
Social Security Administration	8.9	8.0
Pension Benefit Guaranty Corporation	8.4	5.8
Department of Defense	7.8	7.5
Department of Health and Human Services	7.4	13.0
Department of Energy	4.0	3.9
Tennessee Valley Authority	3.0	1.7
Department of the Treasury	1.9	1.7
Department of Veterans Affairs	1.8	1.3
Department of the Interior	1.6	1.9
Office of Personnel Management	1.2	1.0
All other departments	5.8	5.2
Accounts receivable, net	61.9	59.9
Taxes Receivable:		
Gross taxes receivable	115.5	101.5
Allowance for doubtful accounts	(84.4)	(73.6)
Taxes receivable, net	31.1	27.9
Total accounts and taxes receivable, net	93.0	87.8

Accounts receivable includes related interest receivable of $6.4 billion and $6.3 billion as of September 30, 2008, and 2007, respectively. Accounts receivable are net of an allowance for uncollectible accounts. The allowance amounts are $15.2 billion and $14.3 billion as of September 30, 2008, and 2007, respectively.

Accounts receivable for Health and Human Services (HHS) decreased by $5.6 billion primarily due to the Medicare Prescription Drug Program for the year ending September 30, 2008.

Note 4. Loans Receivable and Loan Guarantee Liabilities, Net

Direct Loan and Defaulted Guaranteed Loan Programs as of September 30

(In billions of dollars)	Face Value of Loans Outstanding		Long-term Cost of Direct Loans and Defaulted Guaranteed Loans Outstanding		Loans Receivable, Net		Subsidy Expense for the Fiscal Year	
	2008	2007	2008	2007	2008	2007	2008	2007
Federal Direct Student Loans - Education	124.4	108.0	14.2	8.7	110.2	99.3	5.2	(0.5)
Electric Loans - USDA	37.5	36.0	2.0	1.2	35.5	34.8	0.5	-
Federal Family Education Loans - Education	32.7	23.7	8.2	7.2	24.5	16.5	(0.2)	-
Rural Housing Services - USDA	27.6	27.1	7.0	6.9	20.6	20.2	0.3	0.1
Water and Environmental Loans - USDA	9.9	9.3	0.9	0.7	9.0	8.6	0.2	-
Disaster Loan Programs - SBA	8.6	9.0	1.5	1.5	7.1	7.5	-	-
Farm Loans - USDA	6.7	6.6	(0.4)	0.3	7.1	6.3	(0.4)	-
Housing and Urban Development Loans	4.9	3.9	(0.8)	(0.9)	5.7	4.8	1.1	(0.2)
Telecommunications Loans - USDA	4.0	4.0	(0.1)	(0.3)	4.1	4.3	0.2	(0.1)
U.S. Agency for International Development Loans	6.3	6.7	2.3	2.3	4.0	4.4	-	5.9
Food Aid - USDA	6.7	7.6	2.8	3.5	3.9	4.1	(0.3)	-
Housing for the Elderly and Disabled - HUD	3.9	4.6	-	-	3.9	4.6	-	-
Export-Import Bank Loans	6.4	7.3	2.6	2.9	3.8	4.4	-	-
GSE Mortgage Backed Securities Purchase Program - Treasury	3.3	-	(0.1)	-	3.4	-	(0.1)	-
All Other Programs	25.1	16.0	4.5	3.9	20.6	12.1	0.4	0.4
Total Direct Loans and Defaulted Guaranteed Loans	308.0	269.8	44.6	37.9	263.4	231.9	6.9	5.6

Loan Guarantees as of September 30

(In billions of dollars)	Principal Amount of Loans under Guarantee		Principal Amount Guaranteed by the United States		Loan Guarantee Liabilities		Subsidy Expense for the Fiscal Year	
	2008	2007	2008	2007	2008	2007	2008	2007
Federal Housing Administration Loans - HUD	576.4	438.8	534.9	400.0	19.6	7.4	(1.0)	(1.0)
Federal Family Education Loans - Education	414.6	363.3	405.2	359.2	43.2	50.8	(2.7)	4.9
Small Business Loans - SBA	75.1	71.5	61.7	58.4	1.8	1.7	0.4	-
Export-Import Bank Guarantees	51.8	50.2	51.8	50.2	1.4	1.3	-	0.1
Veterans Housing Benefit Programs - VA	220.8	207.6	36.1	24.9	3.5	3.8	(0.6)	0.1
Rural Housing Services - USDA	22.5	17.9	20.3	16.1	0.8	0.7	0.1	-
Israeli Loan Guarantee Program - AID	12.5	12.7	12.5	12.7	1.2	1.4	-	-
Overseas Private Investment Corporation Credit Program	4.7	4.1	4.7	4.1	0.1	0.5	-	-
Export Credit Guaranteed Programs - USDA	3.9	2.4	3.8	2.3	0.2	0.2	-	(0.3)
Business and Industry Loans - USDA	3.8	3.7	2.8	2.7	0.3	0.3	-	0.1
Federal Ship Financing Fund (Title XI) - DOT	2.4	2.7	2.4	2.9	0.3	0.3	(0.1)	-
All Other Guaranteed Loan Programs	14.2	18.5	13.0	16.6	0.5	0.7	-	(0.1)
Total Loan Guarantees	1,402.7	1,193.4	1,149.2	950.1	72.9	69.1	(3.9)	3.8

Direct loans and loan guarantee programs are used to promote the Nation's welfare by making financing available to segments of the population not served adequately by non-Federal institutions. For those unable to afford credit at the market rate, Federal credit programs provide subsidies in the form of direct loans offered at an interest rate lower than the market rate. For those to whom non-Federal financial institutions are reluctant to grant credit because of the high risk involved, Federal credit programs guarantee the payment of these non-Federal loans and absorb the cost of defaults.

The amount of the long-term cost of post-1991 direct loans and loan guarantees outstanding equals the subsidy cost allowance for direct loans and the liability for loan guarantees as of September 30. The amount of the long-term cost of pre-1992 direct loans and loan guarantees equals the allowance for uncollectible amounts (or present value allowance) for direct loans and the liability for loan guarantees. The long-term cost is based on all direct loans and guaranteed loans disbursed in this fiscal year and previous years that are outstanding as of September 30. It includes the subsidy cost of these loans and guarantees estimated as of the time of loan disbursement and subsequent adjustments such as modifications, reestimates, amortizations, and writeoffs.

Net loans receivable includes related interest and foreclosed property, and is included in the assets section of the balance sheets. Foreclosed property is property that is transferred from borrowers to a Federal credit program, through foreclosure or other means, in partial or full settlement of post-1991 direct loans or as a compensation for losses that the Government sustained under post-1991 loan guarantees. Please refer to the individual financial statements of the Department of Veterans Affairs (VA) and the Department of Housing and Urban Development (HUD) for significant detailed information regarding foreclosed property.

The total subsidy expense is the cost of direct loans and loan guarantees recognized during the fiscal year. It consists of the subsidy expense incurred for direct and guaranteed loans disbursed during the fiscal year, for modifications made during the fiscal year of loans and guarantees outstanding, and for reestimates as of the end of the fiscal year of the cost of loans and guarantees outstanding. This expense is included in the Statements of Net Cost.

Major Loan Programs

The Department of Education (Education) has two major education loan programs. The first program, the Federal Direct Student Loan Program, established in fiscal year 1994, offers four types of education loans: Stafford, Unsubsidized Stafford, PLUS for parents, and consolidation loans. Evidence of financial need is required for a student to receive a subsidized Stafford loan. The other three types of loans are available to borrowers at all income levels. These loans usually mature 9 to 13 years after the student is no longer enrolled. They are unsecured. The second program, the Federal Family Education Loan Program, established in fiscal year 1965, is a guaranteed loan program. Like the Federal Direct Student Loan Program, it offers four types of loans: Stafford, Unsubsidized Stafford, PLUS for parents, and consolidation loans.

The Department of Agriculture (USDA) offers direct and guaranteed loans through credit programs in the Farm and Foreign Agricultural Services (FFAS) mission area through the Farm Service Agency (FSA), and the Commodity Credit Corporation (CCC), and in the Rural Development Mission Area (RD).

The FFAS delivers commodity, credit, conservation, disaster and emergency assistance programs that help strengthen and stabilize the agricultural economy.

The FSA offers direct and guaranteed loans to farmers who are temporarily unable to obtain private, commercial credit and through this supervised credit, the goal is to graduate its borrowers to commercial credit. The CCC offers both credit guarantee and direct credit programs for buyers of U.S. exports, suppliers, and sovereign countries in need of food assistance.

The RD provides affordable housing and essential community facilities to rural communities through its rural housing loan and grant programs. These programs include:

- Very low- and low-to-moderate-income home ownership loans and guarantees.
- Very low-income housing repair loans.
- Multi-family housing loans and guarantees.
- Domestic farm labor housing loans.
- Housing site loans.
- Credit sales of acquired property.

The Rural Utilities Program administers a variety of loan programs for electric energy, telecommunications, and water and environmental projects in rural America.

The Department of Housing and Urban Development's, Federal Housing Administration (FHA) provides mortgage insurance to encourage lenders to make credit available to expand home ownership. FHA predominantly serves borrowers that the conventional market does not serve adequately. This includes first-time homebuyers, minorities, low-income families, and residents of under-served areas. Borrowers obtain an FHA insured mortgage and pay an upfront premium and an annual premium to FHA. The proceeds from those premiums are used to fund FHA program costs, including claims on defaulted mortgages and holding costs, property management fees, property sales, and other associated costs. FHA continues to be a financially conservative and stabilizing presence for credit markets in times of economic disruption.

The Small Business Administration's (SBA's) Disaster Assistance Loan Program makes direct loans to disaster victims for the following:

- Loans for homes and personal property.
- Physical disaster loans to business of any size.
- Economic injury loans to small businesses without credit available elsewhere.
- Economic injury loans to eligible businesses affected by essential employees called up to active duty in the military reserves.

The maximum interest rate is 4 percent for applicants without credit available elsewhere and 8 percent for applicants with credit available elsewhere.

The VA's Veterans Housing Benefit Program provides partial guarantee of residential mortgage loans issued to eligible veterans, reservists, and service members by private lenders. This guarantee allows veterans, reservists, and service members to purchase a home without a substantial down payment.

The Export-Import Bank aids in financing and promoting U.S. exports. The average repayment term for these loans is approximately 7 years.

The U.S. Agency for International Development (USAID) provides economic assistance to selected countries in support of U.S. efforts to promote stability and security interests in strategic regions of the world.

Other loan programs include the SBA's general business loan guarantees, the FSA's farm ownership, emergency and disaster loans, and loans and guarantees made by the DOD under its Military Housing Privatization and Armament Retooling and Manufacturing Support Initiative.

Please refer to the individual financial statements of the agencies specified above for significant detailed information regarding their direct and guaranteed loan programs.

MBS Purchase Program

Congress granted Treasury authority to purchase MBS issued by GSE in the Housing and Economic Recovery Act of 2008. The authority expires on December 31, 2009. To promote stability in the mortgage market, Treasury makes MBS purchases in the open market. GSE MBS are credit-guaranteed by the GSE and Treasury plans to hold its portfolio of MBS to maturity unless, based on mortgage market conditions, sales are necessary. This program was implemented to help improve the availability of mortgage credit to American homebuyers and mitigate pressures on mortgage rates. By purchasing these securities, Treasury seeks to broaden access to mortgage funding for current and prospective homeowners, as well as to promote market stability. The scale of the program will be based on developments in the capital markets and housing markets.

The MBS program is accounted for under the provisions of the Federal Credit Reform Act, section 13201 of the Omnibus Budget Reconciliation Act of 1990, P.L. No. 101-508, dated November 5, 1990. Treasury develops subsidy estimates, re-estimates, and rates based on anticipated cashflows from the purchases of MBS. Factors that impact these cashflows and the subsidy rate include the interest coupons on the securities, the discount or premium paid at the time of purchase, the speed of mortgage prepayments, and the probability of GSE failure. A positive subsidy reflects the cost to the Government of the program and a negative subsidy reflects earnings on the program. The fiscal year 2008 GSE MBS subsidy rate was negative, indicating Treasury expects to earn a return on its investments in these securities. As of September 30, 2008, the Treasury agent responsible for MBS purchases was in receipt of $1.7 billion that was recorded as an advance. This amount was to purchase MBS but had not been purchased at yearend and was not made until after September 30, 2008.

GSE Credit Facility Program

Congress granted Treasury authority to make credit available to GSE in the Housing and Economic Recovery Act of 2008. The GSE credit facility program (GSECF) will offer liquidity if needed until December 31, 2009. This will ensure credit availability to GSE and provide secured funding on an as needed basis under terms and conditions established by the Secretary of Treasury to protect taxpayers. Fannie Mae, Freddie Mac, and the Federal Home Loan Banks are eligible to borrow under this program if needed. Funding will be provided directly by Treasury in exchange for eligible collateral from the GSE which will be limited to guaranteed MBS issued by Freddie Mac and Fannie Mae, as well as advances made by the Federal Home Loan Banks. All such assets pledged against loans will be accepted with appropriate collateral margins as determined by Treasury. Loan requests will require approval from Treasury and verification that adequate collateral has been pledged.

The GSECF program is accounted for under the provisions of the Federal Credit Reform Act, section 13201 of the Omnibus Budget Reconciliation Act of 1990, P.L. No. 101-508, dated November 5, 1990. Treasury develops subsidy estimates, re-estimates, and rates based on anticipated cashflows from the credit facility. Factors that impact these cashflows and the subsidy rate include the interest rate on loans and the probability of GSE failure. A positive subsidy reflects the cost to the Government of the program and a negative subsidy reflects earnings on the program. The GSECF was not utilized in fiscal year 2008 and no loans were made.

Note 5. Inventories and Related Property, Net

Inventories and Related Property as of September 30

(In billions of dollars)	Defense	All Others	Total	Defense	All Others	Total
		2008			2007	
Inventory purchased for resale	101.1	0.8	101.9	86.5	0.7	87.2
Inventory and operating material and supplies held for repair	44.1	0.6	44.7	48.5	0.6	49.1
Inventory—excess, obsolete, and unserviceable	7.8	-	7.8	7.3	-	7.3
Operating materials and supplies held for use	131.7	4.9	136.6	124.0	5.8	129.8
Operating materials and supplies held in reserve for future use	-	0.2	0.2	-	0.2	0.2
Operating materials and supplies—excess, obsolete, and unserviceable	3.6	0.2	3.8	2.4	0.2	2.6
Stockpile materials	-	46.1	46.1	-	43.9	43.9
Stockpile materials held for sale	0.7	0.2	0.9	0.9	0.3	1.2
Other related property	0.7	1.0	1.7	0.6	1.0	1.6
Allowance for loss	(53.7)	(0.4)	(54.1)	(45.3)	(0.5)	(45.8)
Total inventories and related property, net	236.0	53.6	289.6	224.9	52.2	277.1

Inventory is tangible personal property that is (1) held for sale, principally to Federal agencies, (2) in the process of production for sale, or (3) to be consumed in the production of goods for sale or in the provision of services for a fee.

Inventory purchased for resale is the cost or value of tangible personal property purchased by an agency for resale. DOD values approximately 65 percent of its resale inventory using the moving average cost (MAC) method. An additional 15 percent (fuel inventory) is reported using the first-in-first-out method. DOD reports the remaining 20 percent of resale inventories at an approximation of historical cost using latest acquisition cost (LAC) adjusted for holding gains and losses.

Inventory and operating materials and supplies held for repair are damaged inventory that require repair to make them suitable for sale (inventory) or is more economic to repair than to dispose of (operating materials and supplies).

Inventory—excess, obsolete, and unserviceable consists of:

- Excess inventory is inventory that exceeds the demand expected in the normal course of operations and which does not meet management's criteria to be held in reserve for future sale.
- Obsolete inventory is inventory that is no longer needed due to changes in technology, laws, customs, or operations.
- Unserviceable inventory is inventory damaged beyond economic repair.

Excess, obsolete, and unserviceable inventory is reported at net realizable value.

Please refer to the individual financial statements of DOD and the General Services Administration (GSA) for significant detailed information regarding inventory held for future sale.

Operating materials and supplies held for use are tangible personal property to be consumed in normal operations.

Operating materials and supplies held in reserve for future use are materials retained because they are not readily available in the market or because they will not be used in the normal course of operations, but there is more than a remote chance they will eventually be needed. DOD, which accounts for most of the reported operating materials and supplies held for use, uses LAC, MAC and Standard Price under the purchase and consumption methods of accounting and does not adjust for holding gains and losses. The DOD valuation methods do not approximate historical cost.

Operating materials and supplies—excess, obsolete, and unserviceable consists of:

- Excess operating materials and supplies are materials that exceed the demand expected in the normal course of operations, and do not meet management's criteria to be held in reserve for future use.
- Obsolete operating materials and supplies are materials no longer needed due to changes in technology, laws, customs, or operations.
- Unserviceable operating materials and supplies are materials damaged beyond economic repair.

DOD, which accounts for most of the reported excess, obsolete, and unserviceable operating materials and supplies, revalues it to a net realizable value of zero through the allowance account.

Please refer to the individual financial statements of DOD and NASA for significant detailed information regarding operating materials and supplies.

Stockpile materials include strategic and critical materials held in reserve for use in national defense, conservation, or national emergencies due to statutory requirements; for example, nuclear materials and oil, and stockpile materials that are authorized to be sold. The majority of the amount reported by the DOD is stockpile materials held for sale, and the amount reported by others is stockpile materials held in reserve, with the majority of it being reported by the Department of Energy (DOE). Please refer to their individual financial statements for more information on stockpile materials.

Other related property consists of:

- Commodities include items of commerce or trade that have an exchange value used to stabilize or support market prices. Please refer to the financial statements of the USDA for detailed information regarding commodities.
- Seized monetary instruments are comprised only of monetary instruments that are awaiting judgment to determine ownership. The related liability is included in other liabilities. Other property seized by the Government, such as real property and tangible personal property, is not considered a Government asset. It is accounted for in agency property-management records until the property is forfeited, returned, or otherwise liquidated. Please refer to the individual financial statements of the Department of Justice (Justice), Treasury, and the Department of Homeland Security (DHS) for significant detailed information regarding seized property.
- Forfeited property is comprised of monetary instruments, intangible property, real property, and tangible personal property acquired through forfeiture proceedings; property acquired by the Government to satisfy a tax liability; and unclaimed and abandoned merchandise. Please refer to the individual financial statements of Justice, Treasury, and DHS for significant detailed information regarding forfeited property.
- Foreclosed property is comprised of assets received in satisfaction of a loan receivable or as a result of payment of a claim under a guaranteed or insured loan (excluding commodities acquired under price support programs). All properties included in foreclosed property are assumed to be held for sale. Please refer to the individual financial statements of USDA and HUD for significant detailed information regarding foreclosed property.
- Other property not classified above.

Note 6. Property, Plant, and Equipment, Net

Property, Plant, and Equipment as of September 30, 2008

(In billions of dollars)	Cost		Accumulated Depreciation/ Amortization		Net	
	Defense	All Others	Defense	All Others	Defense	All Others
Buildings, structures, and facilities	180.2	193.3	105.3	99.6	74.9	93.7
Furniture, fixtures, and equipment	789.5	156.5	386.7	91.5	402.8	65.0
Construction in progress	22.5	39.0	N/A	N/A	22.5	39.0
Land	10.5	11.7	N/A	N/A	10.5	11.7
Internal use software	8.9	12.8	5.5	5.9	3.4	6.9
Assets under capital lease	1.0	2.0	0.5	0.8	0.5	1.2
Leasehold improvements	0.6	4.9	0.4	2.6	0.2	2.3
Other property, plant, and equipment	0.1	8.6	-	5.6	0.1	3.0
Subtotal	1,013.3	428.8	498.4	206.0	514.9	222.8
Total property, plant, and equipment, net		1,442.1		704.4		737.7

Property, Plant, and Equipment as of September 30, 2007

(In billions of dollars)	Cost		Accumulated Depreciation/ Amortization		Net	
	Defense	All Others	Defense	All Others	Defense	All Others
Buildings, structures, and facilities	173.3	189.3	101.5	96.9	71.8	92.4
Furniture, fixtures, and equipment	728.1	151.0	359.7	84.5	368.4	66.5
Construction in progress	19.5	34.5	N/A	N/A	19.5	34.5
Land	10.5	11.3	N/A	N/A	10.5	11.3
Internal use software	9.3	10.6	5.8	4.9	3.5	5.7
Assets under capital lease	1.0	1.7	0.5	0.7	0.5	1.0
Leasehold improvements	0.6	4.4	0.3	2.4	0.3	2.0
Other property, plant, and equipment	0.1	8.6	-	5.5	0.1	3.1
Subtotal	942.4	411.4	467.8	194.9	474.6	216.5
Total property, plant, and equipment, net		1,353.8		662.7		691.1

For physical quantity information related to multi-use heritage assets, refer to Note 24—Stewardship Land and Heritage Assets.

DOD comprises approximately 70 percent of the Government's reported property, plant, and equipment as of September 30, 2008. Refer to the individual financial statements of DOD, DOE, the Tennessee Valley Authority (TVA), the United States Postal Service (USPS), NASA, and GSA for significant detailed information on the useful lives and related capitalization thresholds for property, plant, and equipment. These agencies comprise 86 percent of the Government's total reported net property, plant, and equipment of $737.7 billion as of September 30, 2008.

Note 7. Securities and Investments

Securities and Investments as of September 30, 2008

By Category

(In billions of dollars)	Held-To-Maturity			Trading Securities			
	Cost Basis	Unamortized Premium/ Discount	Net Invest-ment	Cost Basis	Unrealized Gain/Loss	Net Invest-ment	Total
Fixed/debt securities:							
Non-U.S. Government	10.8	-	10.8	2.9	(0.3)	2.6	13.4
Commercial	-	-	-	(0.2)	-	(0.2)	(0.2)
Mortgage/asset backed	0.2	-	0.2	3.8	(0.4)	3.4	3.6
Corporate and other bonds	-	-	-	13.4	(2.3)	11.1	11.1
All other fixed debt securities	-	-	-	0.2	(0.1)	0.1	0.1
Equity securities:							
Common stocks	-	-	-	3.6	(0.7)	2.9	2.9
Unit trust	-	-	-	6.2	3.4	9.6	9.6
All other equity securities	-	-	-	1.1	(0.1)	1.0	1.0
Other	2.1	-	2.1	36.0	-	36.0	38.1
Total Securities and Investments	13.1	-	13.1	67.0	(0.5)	66.5	79.6

Securities and Investments as of September 30, 2007

By Category

(In billions of dollars)	Held-To-Maturity			Trading Securities			
	Cost Basis	Unamortized Premium/ Discount	Net Invest-ment	Cost Basis	Unrealized Gain/Loss	Net Invest-ment	Total
Fixed/debt securities:							
Non-U.S. Government	10.2	0.1	10.3	2.2	-	2.2	12.5
Commercial	-	-	-	1.2	-	1.2	1.2
Mortgage/asset backed	0.2	-	0.2	4.6	-	4.6	4.8
Corporate and other bonds	-	-	-	11.4	(0.2)	11.2	11.2
All other fixed debt securities	-	-	-	4.4	0.2	4.6	4.6
Equity securities:							
Common stocks	-	-	-	3.8	0.6	4.4	4.4
Unit trust	-	-	-	6.3	6.2	12.5	12.5
All other equity securities	-	-	-	1.2	-	1.2	1.2
Other	1.7	-	1.7	45.7	-	45.7	47.4
Total Securities and Investments	12.1	0.1	12.2	80.8	6.8	87.6	99.8

Securities and Investments as of September 30

By Agency

(In billions of dollars)	2008	2007
Securities and Investments:		
Pension Benefit Guaranty Corporation	33.6	45.9
Railroad Retirement Board	24.9	32.0
Exchange Stabilization Fund	10.6	10.0
Tennessee Valley Authority	7.9	9.6
All other	2.6	2.3
Total Securities and Investments	79.6	99.8

These securities and investments do not include nonmarketable Treasury securities, which have been eliminated in consolidation. Held-to-maturity securities and investments are presented at cost, net of unamortized premiums and discounts. Trading securities and investments are presented at fair market value. The Pension Benefit Guaranty Corporation (PBGC) and the Tennessee Valley Authority invest primarily in fixed maturity and equity securities, all classified as trading. The National Railroad Retirement Investment Trust (NRRIT), on behalf of the Railroad Retirement Board, manages and invests railroad retirement assets that are to be used to pay retirement benefits to the Nation's railroad workers under the Railroad Retirement Program. The NRRIT's investments are all classified as other trading equity securities. Treasury's Exchange Stabilization Fund invests primarily in foreign currency, bonds, and bills and are all classified as held-to-maturity. The TVA balance includes $6.9 billion and $8.4 billion as of September 30, 2008, and 2007, respectively, for the Tennessee Valley Authority Retirement System (TVARS). Please refer to the individual financial statements of PBGC, the NRRIT, the Department of the Treasury-Exchange Stabilization Fund, the Tennessee Valley Authority and the TVARS for more detailed information related to securities and investments. These agencies comprise 96.0 percent of the total reported securities and investments of $79.6 billion as of September 30, 2008.

Note 8. Financial and Housing Market Stabilization

Steps Taken to Ensure Financial Stability of GSE

Fannie Mae and Freddie Mac are stockholder-owned GSE. Congress established the GSE to increase stability and housing in the secondary mortgage market. A key Fannie Mae and Freddie Mac business function is to guarantee mortgage-backed securities. These securities are subsequently sold to investors. Proceeds from these sales are used to buy additional mortgages and keep money flowing through the mortgage markets. Fannie Mae and Freddie Mac debt and guaranteed MBS outstanding totaled approximately $5 trillion at September 30, 2008.

Increasingly difficult conditions in the housing market challenged the soundness and profitability of Fannie Mae and Freddie Mac, thereby undermining the entire housing market. This led Congress to pass the Housing and Economic Recovery Act of 2008 in July 2008 (HERA). This Act created the new Federal Housing Finance Agency (FHFA), with enhanced regulatory authority over the GSE, and provided the Secretary of the Treasury with certain authorities intended to ensure the financial stability of the GSE, if necessary.

Due to deteriorating conditions in the housing mortgage markets and the resulting negative financial impact on the GSE, FHFA placed them under conservatorship on September 7, 2008. This action was taken to preserve GSE assets, ensure a sound and solvent financial condition, and mitigate systemic risks that contributed to current market instability.

Pursuant to the authorities provided to the Secretary of the Treasury under the HERA, the Treasury Department, also on September 7, 2008, took three additional steps discussed below to help ensure the solvency and liquidity of the GSE while they are working to resolve their financial difficulties.

Senior Preferred Stock Purchase Agreements

The first step was entering into senior preferred stock purchase agreements with each GSE. In exchange for entering into these agreements, Treasury initially received from each GSE: (1) 1,000,000 shares of non-voting variable liquidation preference senior preferred stock with a liquidation preference value of $1,000 per share and (2) a non-transferrable warrant for the purchase at a nominal cost of 79.9 percent of common stock on a fully-diluted basis. The warrants expire on September 7, 2028. The GSE preferred stock and warrants for common stock were valued as of the initial date at about $7 billion and also valued at September 30, 2008, at about $12 billion. Treasury recorded the investment using the appraisal value ($7 billion) at the date of purchase, September 8, 2008, and then subsequently used the valuation ($12 billion) at the reporting date to determine that no permanent impairment had occurred; therefore, the recorded amount remained at the historical appraised value. Other revenue of about $7 billion was recognized from the acquisition of preferred stock and warrants. As of September 30, 2008, GSE investments consisted of the following items:

GSE Investment

(In billions of dollars)	Appraisal Value At Purchase Date	Unamortized (Premium) Discount	Net Investment	Interest Receivable	9/30/08 Investment Balance	Appraisal Value At Reporting Date
Fannie Mae Senior Preferred Stock	.8	-	.8	-	.8	.7
Freddie Mac Senior Preferred Stock	.8	-	.8	-	.8	.7
Fannie Mae Warrants Common Stock	3.1	-	3.1	-	3.1	6.5
Freddie Mac Warrants Common Stock	2.3	-	2.3	-	2.3	4.4
Total GSE Investment	7.0	-	7.0	-	7.0	12.3

The senior preferred stock accrues dividends at 10 percent per year, payable quarterly. This rate shall increase to 12 percent if, in any quarter, the dividends are not paid in cash, until all accrued dividends have been paid. In addition, beginning on March 31, 2010, the GSE will pay the Treasury Department a periodic commitment fee on a quarterly basis. This commitment fee will compensate the Treasury Department for the explicit support provided by the preferred stock agreements. This fee will be initially set by December 31, 2009, based on mutual agreement between the Treasury Department and each GSE (in practice, the FHFA while the GSE are in conservatorship), in consultation with the Chairman of the Federal Reserve Board. The fee shall be established for 5-year periods, and may be waived by Treasury for one year at a time if warranted by adverse mortgage market conditions. It may be paid in cash or may be added to the liquidation preference.

These agreements, which have no expiration date, provide that Treasury will increase its investment in the senior preferred stock if, at the end of any quarter, the FHFA determines that the liabilities of either GSE exceed its assets. The maximum amount available to each GSE under this agreement is $100 billion. Treasury determined that the net present value of this potential liability cannot be measured with sufficient reliability for fiscal year 2008. Accordingly, the estimated future liability, which would take into account increases in preferred stock liquidation preference, associated dividends, and future commitment fees, is not recorded in the financial statements. Treasury will attempt to make this determination on at least an annual basis going forward.

The actual recorded liability arising from the reported excess of Freddie Mac liabilities over assets (there was no payment anticipated or accrued for Fannie Mae) as of September 30, 2008, is $13.8 billion. This amount is also recorded as an expense for fiscal year 2008. The payment of this liability in fiscal year 2009 will result in an increase to the investment in GSE preferred stock. The carrying value of the investment will be evaluated on at least an annual basis.

GSE Credit Facility (GSECF)

The second step was the establishment of the GSECF to ensure credit availability to Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. This lending facility will provide secured funding on an as needed basis under terms and conditions established by the Secretary of the Treasury to protect taxpayers. The GSECF provides liquidity, if needed, until December 31, 2009.

Funding will be provided directly by Treasury from its account held at the Federal Reserve Bank of New York (FRBNY) in exchange for eligible collateral, which will be limited to guaranteed mortgage backed securities issued by the GSE as well as advances made by the Federal Home Loan Banks. Loan requests will require approval from Treasury and verification by the FRBNY that adequate collateral has been pledged. Loans will be for short-term durations and are in general expected to be for less than one month but no shorter than one week. Loans will not be made with a maturity date beyond December 31, 2009. The rate on a loan request ordinarily will be based on the daily London Interbank Borrowing Rate for a similar term loan plus 50 basis points. The rate is set at the discretion of the Treasury Secretary with the objective of protecting the taxpayer, and is subject to change.

There is no stated limitation on loans provided through the GSECF. However, loans are limited to the amounts of available collateral.

There were no loans made through the GSECF in fiscal year 2008 (see Note 4).

GSE Mortgage-Backed Securities Purchase Program

The third step was the initiation of a temporary program to further support the availability of mortgage financing for millions of Americans and to mitigate pressures on mortgage rates. Under this program, Treasury purchases GSE MBS in the open market. By purchasing these credit-guaranteed securities, Treasury seeks to broaden access to mortgage funding for current and prospective homeowners and to promote stability in the mortgage market.

The size and timing of the MBS purchases is subject to the discretion of the Secretary of the Treasury. The scale of the program will be based on developments in the capital and housing markets. Initial purchases of $3.3 billion were made during September 2008. Purchases continued into fiscal year 2009, and additional purchases will be made as deemed appropriate through the expiration of this authority on December 31, 2009.

As these securities are backed by individual mortgages, they are accounted for under the Credit Reform Act of 1990 and are included in Note 4.

Temporary Guarantee Program for Money Market Funds

Treasury has established a Temporary Guarantee Program (Program) for Money Market Funds. Under this Program the Treasury Department will guarantee to investors that they will receive the stable share price (SSP) for shares held in participating money market funds as of the close of business on September 19, 2008. President George W. Bush approved the use of existing authorities by Secretary Henry M. Paulson, Jr. to make available, as necessary, the assets of the ESF to support the Program. If a participating fund’s market-based net asset value (NAV) falls below 99.5 percent of the SSP and is not cured, a Guarantee Event will be deemed to occur. If outlays become necessary, they would be paid out initially from the ESF, and then under the provisions of Section 131 of the Emergency Economic Stabilization Act of 2008, such outlays would be reimbursed from funds available under the Troubled Asset Relief Program (Note 25).

Eligible funds must be regulated under Rule 2a-7 of the Investment Company Act of 1940, must maintain a SSP, must have had a market-based NAV of at least 99.5 percent of the SSP as of September 19, 2008, and must be publicly offered and registered with the Securities and Exchange Commission. The program was to be in effect until December 18, 2008, but was subsequently extended to April 30, 2009, with an option to extend until September 18, 2009, at the discretion of the Secretary of the Treasury.

To participate in the Program, eligible money market funds must submit an application and pay a premium of 1 basis point if the fund’s NAV is greater than or equal to 99.75 percent of the SSP, or 1.5 basis points of the SSP if the fund’s NAV is less than 99.75 percent of the SSP but greater than or equal to 99.50 percent of the SSP. With the extension of the program beyond December 18, 2008, new premium charges apply and funds have the option to renew their coverage.

As of September 30, 2008, Treasury collected $39.7 million in program participation premiums. As of October 10, 2008, Treasury collected an additional $298.1 million in premiums. These premiums represent the payments for the first three months of coverage which began September 19, 2008. All premium payments were invested into U.S. Government securities. The program currently covers over $3 trillion of assets. Program participation payments from funds that are not accepted into the Program will be returned. Of the total $337.8 million collected, $45.0 million was recognized as earned revenue, while $292.8 million remained as unearned revenue at September 30, 2008.

The Government’s exposure under the Program, when a guarantee event occurs, is the difference between the SSP and the NAV at liquidation of the money market fund. The Government believes the risk of loss under the Program is negligible, and no future liability is recorded at September 30, 2008.

Note 9. Other Assets

Other Assets as of September 30

(In billions of dollars)	**2008**	**2007**
Advances and prepayments	43.9	30.5
Other	36.0	34.9
Total other assets	79.9	65.4

Advances and prepayments are assets that represent funds disbursed in contemplation of the future performance of services, receipt of goods, the incurrence of expenditures, or the receipt of other assets. These include advances to contractors and grantees, travel advances, and prepayments for items such as rents, taxes, insurance, royalties, commissions, and supplies.

Other items included in other assets are regulatory assets, purchased power generating capacity, deferred nuclear generating units, nonmarketable equity investments in international financial institutions, the balance of assets held by the experience-rated carriers participating in the Health Benefits and Life Insurance Program (pending disposition on behalf of Office of Personnel Management (OPM)), and receivables from bank and thrift resolutions.

With regard to regulatory assets, the Department of Energy's Power Marketing Authorities (PMAs) and the Tennessee Valley Authority (TVA) record certain amounts as assets in accordance with SFAS No. 71, *Accounting for the Effects of Certain Types of Regulation*. The provisions of SFAS No. 71 require that regulated enterprises reflect rate actions of the regulator in their financial statements, when appropriate. These rate actions can provide reasonable assurance of the existence of an asset, reduce or eliminate the value of an asset, or impose a liability on a regulated enterprise. In order to defer incurred costs under SFAS No. 71, a regulated entity must have the statutory authority to establish rates that recover all costs, and those rates must be charged to and collected from customers. If the PMAs' or TVA's rates should become market-based, SFAS No. 71 would no longer be applicable, and all of the deferred costs under that standard would be expensed. As of September 30, 2008, and 2007, DOE and TVA total regulatory assets are $12.0 billion and $10.7 billion, respectively.

Note 10. Accounts Payable

Accounts Payable as of September 30

(In billions of dollars)	2008	2007
Department of Defense	32.1	29.7
Department of Veterans Affairs	6.2	3.9
Department of the Treasury	3.8	2.5
Tennessee Valley Authority	3.2	2.7
Department of Homeland Security	2.9	3.0
Department of State	2.8	2.0
Federal Deposit Insurance Corporation	2.6	-
Department of Justice	2.1	2.8
General Services Administration	2.1	1.8
Agency for International Development	1.9	2.4
U.S. Postal Service	1.7	2.0
Department of Energy	1.6	1.4
National Aeronautics and Space Administration	1.4	1.0
Department of Education	1.3	0.9
Department of the Interior	1.0	1.1
All other	6.6	9.0
Total accounts payable	73.3	66.2

Accounts payable includes amounts due for goods and property ordered and received, services rendered by other than Federal employees, and accounts payable for cancelled appropriations.

Note 11. Federal Debt Securities Held by the Public and Accrued Interest

Federal Debt Securities Held by the Public and Accrued Interest

(In billions of dollars)	Balance September 30, 2007	Net Change During Fiscal Year 2008	Balance September 30, 2008	Average Interest Rate 2008	Average Interest Rate 2007
Treasury securities (public):					
Marketable securities:					
Treasury bills	954.6	529.7	1,484.3	1.6%	4.6%
Treasury notes	2,456.1	167.3	2,623.4	4.1%	4.4%
Treasury bonds	560.9	17.6	578.5	7.1%	7.4%
Treasury inflation-protected securities (TIPS)	456.8	67.2	524.0	2.0%	2.3%
Total marketable Treasury securities	4,428.4	781.8	5,210.2		
Nonmarketable securities	620.9	(22.4)	598.5	4.1%	4.9%
Net unamortized premium/ (discounts)	(39.4)	3.3	(36.1)		
Total Treasury securities, net (public)	5,009.9	762.7	5,772.6		
Agency securities:					
Tennessee Valley Authority	22.6	-	22.6		
All other agencies	0.4	-	0.4		
Total agency securities, net of unamortized premiums and discounts	23.0	-	23.0		
Accrued interest payable	44.8	(4.2)	40.6		
Total Federal debt securities held by the public and accrued interest	5,077.7	758.5	5,836.2		

Types of marketable securities:
Bills – Short-term obligations issued with a term of 1 year or less.
Notes – Medium-term obligations issued with a term of at least 1 year, but not more than 10 years.
Bonds – Long-term obligations of more than 10 years.
TIPS – Term of more than 5 years.

Federal debt securities held by the public outside the Government are held by individuals, corporations, State or local governments, Federal Reserve banks, foreign governments, and central banks. The above table details Government borrowing primarily to finance operations and shows marketable and nonmarketable securities at face value less net unamortized discounts including accrued interest.

Securities that represent Federal debt held by the public are issued primarily by the Treasury and include:

- Interest-bearing marketable securities (bills, notes, bonds, and inflation-protected).
- Interest-bearing nonmarketable securities (foreign series, State and local government series, domestic series, and savings bonds).
- Non interest-bearing marketable and nonmarketable securities (matured and other).

Section 3111 of Title 31, United States Code (U.S.C.) authorizes the Secretary of the Treasury to use money received from the sale of an obligation and other money in the General Fund of the Treasury to buy, redeem, or refund, at or before maturity, outstanding bonds, notes, certificates of indebtedness, Treasury bills, or savings certificates of the Government. There were no buyback operations in fiscal years 2008 and 2007.

Over the course of fiscal year 2008, changes in economic conditions, financial markets, and fiscal policy as well as a reduction in nonmarketable debt issuance have caused an increase in the Government's marketable borrowing needs. Financial market strains have impacted the real economy, and the nation has experienced lower economic growth, lower receipts, and increased outlays. The Government has responded to the increase in marketable borrowing requirements by increasing issuance sizes of regular bills, the frequency, terms, and issuance sizes of cash management bills, and the issuance sizes of nominal coupon security offerings.

As of September 30, 2008, and 2007, respectively, $9,959.9 billion and $8,921.3 billion of debt were subject to a statutory limit (31 U.S.C. § 3101). That limit was $10,615.0 billion as of September 30, 2008, and $9,815.0 billion as of September 30, 2007. The debt subject to the limit includes Treasury securities held by the public and Government guaranteed debt of Federal agencies (shown in the table above) and intragovernmental debt holdings (shown in the following table).

Intragovernmental Debt Holdings: Federal Debt Securities Held as Investments by Government Accounts as of September 30

(In billions of dollars)	Balance 2007	Net Change During Fiscal Year 2008	Balance 2008
Social Security Administration, Federal Old-Age and Survivors Insurance	1,968.3	182.4	2,150.7
Office of Personnel Management, Civil Service Retirement and Disability	701.7	27.1	728.8
Department of Health and Human Services, Federal Hospital Insurance	319.4	(0.7)	318.7
Social Security Administration, Federal Disability Insurance	213.8	2.7	216.5
Department of Defense, Military Retirement Fund	190.2	25.7	215.9
Department of Defense, Medicare-Eligible Retiree Health Care Fund	92.2	20.5	112.7
Department of Labor, Unemployment Trust Fund	74.9	(2.5)	72.4
Department of Health and Human Services, Federal Supplementary Medical Insurance Trust Fund	39.2	19.9	59.1
Department of Energy, Nuclear Waste Disposal Fund	39.4	3.2	42.6
Office of Personnel Management, Employees' Life Insurance	33.0	1.4	34.4
Federal Deposit Insurance Corporation Funds	50.7	(17.4)	33.3
Office of Personnel Management, Postal Service Retiree Health Benefits Fund	25.5	6.8	32.3
Pension Benefit Guaranty Corporation Fund	35.8	(13.4)	22.4
Housing and Urban Development, Federal Housing Administration (FHA) - Liquidating Account	22.4	(3.3)	19.1
Department of the Treasury, Exchange Stabilization Fund	16.4	0.4	16.8
Office of Personnel Management, Employees' Health Benefits	15.9	(0.3)	15.6
Department of State, Foreign Service Retirement and Disability Fund	14.4	0.5	14.9
Department of Transportation, Highway Trust Fund	12.2	0.6	12.8
All other programs and funds	93.0	4.0	97.0
Subtotal	3,958.4	257.6	4,216.0
Unamortized net (discounts)/premiums	3.7	28.9	32.6
Total intragovernmental debt holdings, net	3,962.1	286.5	4,248.6

Intragovernmental debt holdings represent the portion of the gross Federal debt held as investments by Government entities such as trust funds, revolving funds, and special funds. This includes trust funds that are earmarked funds. For more information on earmarked funds, see Note 21─Earmarked Funds. These intragovernmental debt holdings are eliminated in the consolidation of these financial statements.

Note 12. Federal Employee and Veteran Benefits Payable

Federal Employee and Veteran Benefits Payable as of September 30

(In billions of dollars)	Civilian		Military		Total	
	2008	2007	2008	2007	2008	2007
Pension and accrued benefits	1,454.8	1,386.3	1,154.1	1,028.8	2,608.9	2,415.1
Post-retirement health and accrued benefits	341.8	311.6	820.6	835.9	1,162.4	1,147.5
Veterans compensation and burial benefits	N/A	N/A	1,466.7	1,127.7	1,466.7	1,127.7
Life insurance and accrued benefits	37.5	35.9	12.6	13.1	50.1	49.0
FECA benefits	16.6	15.9	8.8	8.7	25.4	24.6
Liability for other benefits	0.4	0.5	5.0	4.7	5.4	5.2
Total Federal employee and veteran benefits payable	1,851.1	1,750.2	3,467.8	3,018.9	5,318.9	4,769.1

Change in Pension and Accrued Benefits

(In billions of dollars)	Civilian	Military	Total
Actuarial accrued pension liability as of September 30, 2007	1,386.3	1,028.8	2,415.1
Pension Expense:			
Prior (and past) service costs from plan amendments	-	8.1	8.1
Assumption changes	0.2	60.1	60.3
Normal costs	28.0	18.7	46.7
Interest on pension liability during the period	84.8	60.8	145.6
Actuarial (gains)/losses	21.6	23.3	44.9
Total pension expense	134.6	171.0	305.6
Less benefits paid	66.1	45.7	111.8
Actuarial accrued pension liability as of September 30, 2008	1,454.8	1,154.1	2,608.9

Change in Post-Retirement Health and Accrued Benefits

(In billions of dollars)	Civilian	Military	Total
Actuarial accrued post-retirement health benefits liability, as of September 30, 2007	311.6	833.8	1,145.4
Reclassification from liability for other benefits	-	2.1	2.1
Corrected beginning post-retirement health benefits liability	311.6	835.9	1,147.5
Post-Retirement Health Benefits Expense:			
Normal costs	12.4	20.8	33.2
Interest on liability	19.9	50.8	70.7
Change in medical inflation rate assumption (gains)/losses	-	(58.1)	(58.1)
Other actuarial (gains)/losses	10.6	(10.0)	0.6
Total post-retirement health benefits expense	42.9	3.5	46.4
Less claims paid	12.7	18.8	31.5
Actuarial accrued post-retirement health benefits liability, as of September 30, 2008	341.8	820.6	1,162.4

The Government offers its employees life and health insurance, as well as retirement and other benefits. The liabilities for these benefits, which include both actuarial amounts, amounts due and payable to beneficiaries and health care carriers, apply to civilian and military employees.

OPM administers the largest civilian plan. DOD administers the largest military plan. Other significant pension plans with more than $10 billion in accrued benefits payable include those of the Coast Guard and the Foreign Service.

Significant Long-Term Economic Assumptions Used in Determining Pension Liability and the Related Expense

	Civilian		Military	
	2008	2007	2008	2007
Rate of interest	6.25%	6.25%	5.75%	6.00%
Rate of inflation	3.50%	3.50%	3.00%	3.00%
Projected salary increases	4.25%	4.25%	3.75%	3.75%

Significant Long-Term Economic Assumptions Used in Determining Post-Retirement Health Benefits and the Related Expense

	Civilian		Military	
	2008	2007	2008	2007
Rate of interest	6.25%	6.25%	5.75%	6.00%
Rate of health care cost increases	7.00%	7.00%	6.25%	6.25%

Separate boards of actuaries for OPM and DOD approve the actuarial assumptions used in calculating the pension liability and the post-retirement health benefit liability for the civilian and military personnel. The boards use generally accepted actuarial methodologies. The board for OPM uses a fixed rate of inflation and projected salary increases over all years for both the pension and post-retirement health benefit liabilities. These rates are shown in the tables above. OPM approves the long term assumptions for interest, inflation, and across-the-board salary increases shown in the table above. The DOD Board approves the assumptions used for the Medicare-eligible portion of the military post-retirement health benefit liabilities. DOD uses a range of rates for the health care cost inflation increases, varying by year and type of service, with an ultimate rate for the long-term as shown in the table above.

The long-term ultimate rate for fiscal year 2008 of 6.25 percent is shown in the tables above. For disclosure and comparison purposes, DOD's estimate of a single equivalent fixed rate of health care cost inflation for fiscal year 2008 is 6.5 percent, which is an approximation of the single equivalent rate that would produce that same actuarial liability as the actual rates used.

Civilian Employees

Pensions

OPM administers the largest civilian pension plan, which covers approximately 90 percent of all Federal civilian employees. This plan includes two components of defined benefits. These are the Civil Service Retirement System (CSRS) and the Federal Employees' Retirement System (FERS). The basic benefit components of the CSRS and the FERS are financed and operated through the Civil Service Retirement and Disability Fund (CSRDF).

CSRDF monies are generated primarily from employees' contributions, agency contributions, payments from the General Fund, and interest on investments in Treasury securities. See Note 21—Earmarked Funds.

The Federal Retirement Thrift Investment Board administers the Thrift Savings Plan (TSP) Fund. The TSP Fund investment options include two fixed income funds (the G and F Funds), three stock funds (the C, S, and I Funds) and five lifecycle funds (L 2040, L 2030, L 2020, L 2010, and L Income). The L-Funds, established August 1, 2005, diversifies participant accounts among the G, F, C, S, and I Funds, using professionally determined investment mixes (allocations) that are tailored to different time horizons. These financial statements exclude the TSP because the CSRS and FERS employees own its assets.

Treasury securities held in the G-Fund are included in total Federal debt securities held by the public and accrued interest in the balance sheets. The G-Fund held $101.5 billion and $81.4 billion in nonmarketable Treasury securities as of September 30, 2008, and 2007, respectively (Note 11).

Post-Retirement Health Benefits

The post-retirement civilian health benefit liability is an estimate of the Government's future cost of providing post-retirement health benefits to current employees and retirees. Although active and retired employees pay insurance premiums under the Federal Employees Health Benefits Program, these premiums cover only a portion of the costs. The OPM actuary applies economic assumptions to historical cost information to estimate the liability, which is then reduced by certain operating costs and premiums received during the year.

Life Insurance Benefits

One of the largest other employee benefits is the Federal Employee Group Life Insurance Program. Employee and annuitant contributions and interest on investments fund a portion of this liability. The actuarial life insurance liability is the expected present value of future benefits to pay to, or on behalf of, existing Life Insurance Program participants. The OPM actuary uses interest rate, inflation, and salary increase assumptions that are consistent with the pension liability.

Workers' Compensation Benefits

The Department of Labor (DOL) determines both civilian and military agencies' liabilities for future workers' compensation benefits for civilian Federal employees, as mandated by the Federal Employees Compensation Act (FECA) for death, disability, medical, and miscellaneous costs for approved compensation cases, and a component for incurred, but not reported, claims. The FECA liability is determined annually using historical benefit payment patterns related to a specific incurred period to predict the final payment related to the period. These estimated payments have been discounted to present value using the Office of Management and Budget's economic assumptions for 10-year U.S. Treasury notes and bonds. For 2008, a 4.37 percent interest rate was assumed and 4.77 percent was assumed for year two and thereafter.

The DOL calculates the FECA liability using wage inflation factors (cost of living adjustments or COLA) and medical inflation factors (consumer price index – medical or CPIM). The table below reflects the compensation COLAs and CPIMs used in the estimations for various charge back years.

Fiscal Year	COLA	CPIM
2009	3.87%	4.01%
2010	2.73%	3.86%
2011	2.20%	3.87%
2012	2.23%	3.93%
2013+	2.30%	3.93%

Military Employees (Including Veterans)

Pensions

The DOD Military Retirement Fund (MRF) finances military retirement and survivor benefit programs. The increase in Military Retirement Pension is due to interest on the pension liability, assumption and benefit changes, and experience. The increase due to interest is proportionate to the size of the liability. Liabilities in the future will depend on future benefit changes, assumption changes, and actuarial experience.

Projected revenues into the MRF come from three sources: interest earnings on MRF assets, monthly DOD contributions, and annual contributions from Treasury. In fiscal year 2005, the contributions made by Treasury were increased by an amount equal to the annual expense for the new concurrent receipt provision of the fiscal year 2004 National Defense Authorization Act.

Pension and accrued benefits increased in fiscal year 2008 primarily due to changes in assumptions, benefits and actuarial experience. The key assumption changes were a 0.25 percent interest rate reduction that increased the liability $41.7 billion and changes in retiree and mortality rates which led to an $18.4 billion increase. Actuarial experience, including military pay and cost of living adjustments, led to a $23.3 billion increase, and benefit improvements, primarily an allowance for certain reservists to retire early, led to a $8.1 billion increase. The remaining increase results primarily from an expected increase in the actuarial liability of $34.0 billion (growth due to normal cost, interest cost, and liability released through benefit payments).

The military retirement system consists of a funded, noncontributory, defined benefit plan. It applies to military personnel (Departments of the Army, Navy, Air Force, and Marine Corps). This system includes nondisability retirement pay, disability retirement pay, and survivor annuity programs. Military personnel who remain on active duty for 20 years or longer are eligible for retirement. There are three different retirement benefit formulas that are currently being used by the military: Final Pay, High-3 Year Average, and Career Status Bonus/REDUX. The date each individual enters the military determines which retirement system they would fall under and if they have the option to pick their retirement system. For more information on these benefits, see DOD's websites (http://www.dfas.mil/army2/bonuses/redux.html, and http://www.defenselink.mil/militarypay/retirement/index.html).

Post-Retirement Health Benefits

Military retirees and their dependents are entitled to health care in military medical facilities if a facility can provide the needed care. Prior to becoming Medicare eligible, military retirees and their dependents also are entitled to participate in TRICARE, which reimburses (net of beneficiary copay and deductible requirements) for the cost of health care from civilian providers. TRICARE options are available in indemnity, preferred provider organization (PPO), and health maintenance organization (HMO) designs.

Since fiscal year 2002, TRICARE as second payer to Medicare, covers military retirees and their dependents after they become Medicare eligible. This TRICARE coverage for Medicare eligible beneficiaries requires that the beneficiary enroll in Medicare Part B and is referred to as TRICARE for Life (TFL). Health care under TFL can be obtained from military medical facilities on an "as available" basis or from civilian providers. Military retiree health care actuarial liability figures include costs incurred in military medical facilities, as well as claims paid to civilian providers and certain administrative costs. Costs paid to civilian providers are net of Medicare's portion of the cost.

Chapter 56 of Title 10, U.S.C. created the DOD Medicare-Eligible Retiree Health Care Fund, which became operative on October 1, 2002 (the fund was created in 2000). The purpose of this fund is to account for the health benefits of Medicare-eligible members and former retirees of the Uniformed Services and their eligible dependents who are Medicare eligible. The Fund receives contributions from the Uniformed Services and Treasury, as well as interest earnings on its investments and pays costs incurred in military medical facilities, as well as claims for care provided by civilian providers under TFL, administration costs associated with processing the TFL claims, and premium costs for HMO coverage provided by U.S. Family Health Plans.

In addition to the health care benefits for civilian and military retirees and their dependents, the VA also provides medical care to veterans on an "as available" basis, subject to the limits of the annual appropriations. In accordance with 38 CFR 17.36 (c), VA's Secretary makes an annual enrollment decision that defines the veterans, by priority, who will be treated for that fiscal year subject to change based on funds appropriated, estimated collections, usage, the severity index of enrolled veterans, and changes in cost. VA recognizes the medical care expenses in the period the medical care services are provided. For the time period 2004 through 2008, the average medical cost per year was $30.0 billion.

Veterans Compensation and Burial Benefits

The Government compensates disabled veterans and their survivors. Veterans compensation is payable as a disability benefit or a survivor's benefit. Entitlement to compensation depends on the veteran's disabilities having been incurred in, or aggravated during, active military service; death while on duty; or death resulting from service-connected disabilities, if not on active duty.

Burial benefits include a burial and plot or interment allowance payable for a veteran who, at the time of death, is qualified to receive compensation or a pension, or whose death occurred in a VA facility.

The liability for veterans compensation and burial benefits payable increased by $339.0 billion in fiscal year 2008 and decreased by $26.1 billion in fiscal year 2007. Actuarial assumption changes were the primary reason behind a more than six-fold increase in VA's costs during fiscal year 2008, compared with a relatively meager decrease in fiscal year 2007. The fiscal year 2008 actuarial cost increase was the largest by far at VA in recent years and accounted for approximately 50 percent of the change in total cost across the Government. The major components of this significant change include changes in discount rates, pay adjustments, and estimates of veteran eligibility.

Veterans Compensation and Burial Benefits Payable as of September 30

(In billions of dollars)	2008	2007
Veterans	1,231.9	944.0
Survivors	230.1	179.9
Burial benefits	4.7	3.8
Total veterans compensation and burial benefits payable	1,466.7	1,127.7

Significant Economic Assumptions Used in Determining Veterans Compensation and Burial Benefits as of September 30

	2008	2007
Rate of interest	3.97%	4.67%
Rate of inflation	2.45%	2.31%

Life Insurance Benefits

The largest veterans' life insurance programs consist of the following:

- National Service Life Insurance (NSLI) covers policyholders who served during World War II.
- Veterans Special Life Insurance (VSLI) was established in 1951 to meet the insurance needs of veterans who served during the Korean Conflict and through the period ending January 1, 1957.
- Veterans Reopened Insurance (VRI), which provided a 1-year reopening for insurance coverage in 1965 for those eligible to have obtained NSLI or VSLI and were disabled.

The components of veteran life insurance liability for future policy benefits are presented below.

Veteran Life Insurance Liability as of September 30

(In billions of dollars)	2008	2007
Insurance death benefits:		
NSLI	7.8	8.2
VSLI	1.6	1.6
VRI	0.3	0.3
Other	0.4	0.5
Total death benefits	10.1	10.6
Death benefit annuities	0.1	0.1
Disability income and waiver	0.5	0.5
Insurance dividends payable	1.9	1.9
Total veterans life insurance liability	12.6	13.1

Insurance dividends payable consists of dividends left on deposit with VA, related interest payable, and dividends payable to policyholders.

The VA supervises service members' Group Life Insurance and Veterans' Group Life Insurance programs that provide life insurance coverage to members of the uniformed armed services and veterans who served during the Vietnam era or thereafter. The VA also provides certain veterans and/or their dependents with pension benefits, based on annual eligibility reviews, if the veteran died or was disabled for nonservice-related causes. The actuarial

present value of the future liability for pension benefits is a nonexchange transaction and is not required to be recorded on the balance sheet. The projected amounts of future payments for pension benefits as of September 30, 2008, and 2007, were $97.3 billion and $81.4 billion, respectively.

Note 13. Environmental and Disposal Liabilities

Environmental and Disposal Liabilities as of September 30

(In billions of dollars)	2008	2007
Department of Energy:		
Environmental management program	185.4	188.6
Legacy environmental liabilities - other	51.2	45.8
Active and Surplus Facilities	29.4	29.2
Total Department of Energy	266.0	263.6
Department of Defense:		
Environmental restoration	32.0	33.1
Disposal of weapon systems program	28.8	31.4
Base realignment and closure	5.2	5.1
Environmental corrective other	4.5	2.9
Total Department of Defense	70.5	72.5
All other agencies	6.3	5.9
Total environmental and disposal liabilities	342.8	342.0

During World War II and the Cold War, DOE (or predecessor agencies) developed a massive industrial complex to research, produce, and test nuclear weapons. The nuclear weapons complex included nuclear reactors, chemical-processing buildings, metal machining plants, laboratories, and maintenance facilities.

At all the sites where these activities took place, some environmental contamination occurred. This contamination was caused by the production, storage, and use of radioactive materials and hazardous chemicals, which resulted in contamination of soil, surface water, and groundwater. The environmental legacy of nuclear weapons production also includes thousands of contaminated areas and buildings, and large volumes of waste and special nuclear materials requiring treatment, stabilization, and disposal.

Of those environmental liabilities, this report presents only cleanup costs from Federal operations known to result in hazardous and radioactive waste that the Government is required to clean up by Federal, State, or local statutes and/or regulations. Some of these statutes are: the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA); the Resource Conservation and Recovery Act; the Nuclear Waste Policy Act of 1982, which provides for permanent disposal of the Nation's high-level radioactive waste and spent nuclear fuel; and Public Law No. 105-204, which requires a plan for the conversion of depleted uranium hexafluoride.

DOE is responsible for managing the legacy of contamination from the nuclear weapons complex. The environmental management baseline estimate includes projections of the technical scope, schedule, and costs for environmental restoration; managing nuclear materials waste treatment, storage and disposal activities; and post-cleanup monitoring and stewardship at each installation. The baseline estimate includes costs for related activities such as landlord responsibilities, program management, and legally prescribed grants and cooperative agreements for participation and oversight by Native American tribes, regulatory agencies, and other stakeholders. Active and surplus facilities represent anticipated remediation costs for those facilities that are conducting ongoing operations but ultimately will require stabilization, deactivation, and decommissioning.

Estimated cleanup costs at sites for which there are no current feasible remediation approaches are excluded from the baseline estimates, although applicable stewardship and monitoring costs for these sites are included. Significant projects not included are the nuclear explosion test areas (e.g., Nevada test site).

Estimating DOE's environmental cleanup liability requires making assumptions about future activities and is inherently uncertain. The future course of DOE's environmental management program will depend on a number of fundamental technical and policy choices to be made in the future. The sites and facilities could be restored to a pristine condition suitable for any desirable use, or could be restored to a point where they pose no near-term health risks. Achieving pristine conditions would have a higher cost but may or may not, warrant the costs and potential ecosystem disruption, or be legally required. The environmental estimates include contingency estimates intended to account for the uncertainties associated with the technical cleanup scope of the program.

DOE's environmental liability estimates are dependent on annual funding levels and achievement of work as scheduled. Congressional appropriations at lower than anticipated levels or, unplanned delays in project completion, would cause increases in the estimates.

DOE is also required to recognize closure and post-closure costs for its active and surplus facilities and environmental corrective action costs for current operations. The cleanup cost associated with active and surplus facilities that is allocated to operating periods beyond the balance sheet date is identified as the unrecognized portion. The DOE unrecognized portion of the cleanup cost associated with active and surplus facilities is $698.0 million and $760.0 million for fiscal years 2008 and 2007, respectively. The unrecognized portion of the cleanup cost is recognized over a predetermined period of time.

Please refer to the financial statements of the Department of Energy for significant detailed information regarding DOE's environmental and disposal liabilities, including cleanup costs.

DOD is required by law to adhere to CERCLA and the Superfund Amendment and Reauthorization Act to clean up contamination resulting from waste disposal practices, leaks, spills, and other activities that have created a public health or environmental risk. CERCLA requires DOD to clean up contamination in coordination with regulatory agencies, other responsible parties, and current property owners.

DOD must restore active installations, installations affected by base realignment and closure, and other areas formerly used as defense sites. DOD also bears responsibility for disposal of chemical weapons and environmental costs associated with the disposal of weapons systems (primarily nuclear powered aircraft carriers and submarines). DOD is responsible, as well, for training range and other nonrange unexploded ordnance cleanup.

DOD is currently using two independently validated estimating models, in addition to engineering estimates, to report its environmental liabilities. The models are the Remedial Action Cost Engineering Requirements (RACER) and the Department of Navy Normalization of Data System (NORM). DOD uses the models to estimate cost during the preliminary assessment and initial site investigation phases of restoration projects. Engineering estimates are generally used to estimate cost from the remedial investigation/feasibility phase of the project forward. DOD is also required to recognize closure and post-closure costs for its general property, plant, and equipment and environmental corrective action costs for current operations. The cleanup cost associated with general property, plant, and equipment that is allocated to operating periods beyond the balance sheet date is identified as the unrecognized portion. The DOD unrecognized portion of the cleanup cost associated with general property, plant, and equipment is $1,953.9 million and $1,589.1 million for fiscal years 2008 and 2007, respectively. The unrecognized portion of the cleanup costs is recognized over a predetermined period of time.

Please refer to the financial statements of the DOD for further detailed information regarding DOD's environmental and disposal liabilities, including cleanup costs.

Note 14. Benefits Due and Payable

Benefits Due and Payable as of September 30

(In billions of dollars)	2008	2007
Federal old-age and survivors insurance	46.4	44.1
Federal supplementary medical insurance (Medicare Parts B and D)	24.0	22.2
Federal disability insurance	22.2	21.7
Federal hospital insurance (Medicare Part A)	21.0	19.4
Grants to states for Medicaid	20.4	19.4
Supplemental security income	4.5	4.2
Unemployment insurance	1.6	1.3
All other benefit programs	4.3	1.4
Total benefits due and payable	144.4	133.7

Benefits due and payable are amounts owed to program recipients or medical service providers as of September 30 that have not been paid. For a description of the programs, see the Supplemental Information—Social Insurance section.

Note 15. Insurance Program Liabilities

Insurance Program Liabilities as of September 30

(In billions of dollars)	2008	2007
Insurance program liabilities:		
Pension Benefit Guaranty Corporation - Benefit Pension Plans	60.0	69.2
Federal Deposit Insurance Corporation	12.1	1.8
Department of Homeland Security - National Flood Insurance Program	5.5	1.5
All other insurance programs	0.2	0.2
Total insurance program liabilities	77.8	72.7

Pension Benefit Guaranty Corporation (PBGC) insures pension benefits for participants in covered defined benefit pension plans. As a wholly owned corporation of the U.S. Government, PBGC's financial activity and balances are included in the consolidated financial statements of the U.S. Government. However, under current law, PBGC's liabilities may be paid only from PBGC's assets and not from the General Fund of the Treasury or assets of the Government in general. As of September 30, 2008, PBGC had total liabilities of $74.1 billion, and its total liabilities exceeded its total assets by $11.2 billion. In addition, as discussed in Note 19—Contingencies, PBGC reported reasonably possible contingent losses of about $46.8 billion.

Of the total FDIC amount, $11.7 billion represents the recorded contingent liability and loss provision for Depositor Insured Fund institutions that are likely to fail within one year. The remaining amounts represent pending depositor claims and contingent liabilities for litigation.

The Federal Emergency Management Agency (FEMA) of DHS administers the National Flood Insurance Program (NFIP) in communities that enact and enforce appropriate flood plain management measures. This liability represents an estimate of NFIP losses that are unpaid at the balance sheet date and is based on the loss and loss adjustment expense factors inherent in the NFIP insurance underwriting operations experience and expectations.

In addition, see Note 8 for information regarding Treasury's Temporary Guarantee Program for Money Market Funds. The Government believes the risk of loss under the program is negligible, and no liability is recorded as of September 30, 2008.

Note 16. Other Liabilities

Other Liabilities as of September 30

(In billions of dollars)	2008	2007
Unearned revenue and assets held for others:		
DOE's unearned fees for nuclear waste disposal and other unearned revenue	53.3	33.6
Assets held on behalf of others	46.2	38.7
Subtotal	99.5	72.3
Employee-related liabilities:		
Accrued Federal employees wages and benefits	35.1	31.2
Selected DOE contractors' and D.C. employees' pension benefits	29.2	28.8
Subtotal	64.3	60.0
Subsidies and grants:		
Farm and other subsidies	21.4	17.9
Grant payments due to State and local governments and others	14.6	13.1
Subtotal	36.0	31.0
International monetary liabilities and gold certificates (Note 2)	18.7	20.8
Miscellaneous liabilities:		
Legal and other contingencies	26.6	24.7
Bonneville Power Administration non-Federal power projects and capital lease liabilities, and disposal liabilities	10.2	12.5
Other miscellaneous	42.8	35.1
Subtotal	79.6	72.3
Total other liabilities	298.1	256.4

Other liabilities represent liabilities that are not separately identified on the balance sheet and are presented on a comparative basis by major category.

Unearned Revenue and Assets Held for Others

The Government recognizes a liability when it receives money in advance of providing goods and services or assumes custody of money belonging to others. The Government's unearned revenue from fees DOE has collected from utility companies for the future cost of managing the disposal of nuclear waste is about $25.5 billion and $24.8 billion as of September 30, 2008, and 2007, respectively. The Federal Communications Commission includes deferred revenue of $17.1 billion as of September 30, 2008, for proceeds received from its competitive bidding system for the recovered analog spectrum relating to licenses that have not been granted. Other unearned revenue includes U.S. Postal Service income for such things as prepaid postage, outstanding money orders, and prepaid P.O. Box rentals. Assets held on behalf of others include funds collected in advance and undelivered defense articles. The Foreign Military Sales program holds $36.0 billion and $29.0 billion as of September 30, 2008, and 2007, respectively for articles and services for future delivery to foreign governments.

Employee-Related Liabilities

This category includes amounts owed to employees at yearend and actuarial liabilities for certain non-Federal employees. Actuarial liabilities for Federal employees and veteran benefits are included in Note 12 and are reported on another line on the balance sheet. The largest liability in the employee-related liabilities category is the amount owed at the end of the fiscal year to Federal employees for wages and benefits (including accrued annual leave). In addition, DOE is liable to certain contractors such as the University of California, which operates the Lawrence Livermore National Laboratory, for contractor employee pension and postretirement benefits, which is about $12.3 billion as of September 30, 2008, and 2007. Also, the Government owed about $8.8 billion and $9.0 billion as of September 30, 2008, and 2007, respectively, for estimated future pension benefits of the District of Columbia's judges, police, firefighters, and teachers.

Subsidies and Grants

The Government supports the public good through a wide variety of subsidy and grant programs in such areas as agriculture, medical and scientific research, education, and transportation. Department of Agriculture programs such as the Conservation Reserve, Tobacco Transition Payment, and Direct and Counter-Cyclical Payment programs account for the majority of the subsidies due, about $12.2 billion, and $11.5 billion as of September 30, 2008, and 2007, respectively.

The Government awards hundreds of billions of dollars in grants annually. These include project grants that are competitively awarded for agency-specific projects, such as HHS grants to fund projects to "enhance the independence, productivity, integration and inclusion into the community of people with developmental disabilities." Other grants are formula grants, such as matching grants. Formula grants go to State governments for such things as education and transportation programs. These grants are paid in accordance with distribution formulas that have been provided by law or administrative regulations. Of the total liability reported for grants as of September 30, 2008, and 2007, the Department of Transportation (DOT), Department of Education (Education), and HHS collectively owed their grantees about $11.9 billion and $11.6 billion, respectively. Refer to the financial statements and footnotes of the respective agencies for additional information.

Miscellaneous Liabilities

Some of the more significant liabilities included in this category are for (1) legal and other contingencies (see Note 19—Contingencies), (2) Bonneville Power Administration liability to pay annual budgets of several power projects for its electrical generating capacity, and (3) payables due to derivative contracts and the purchases of securities. In addition, many Federal agencies reported relatively small amounts of miscellaneous liabilities that are not otherwise described.

Note 17. Collections and Refunds of Federal Revenue

Collections of Federal Revenue for the Year Ended September 30, 2008

(In billions of dollars)	Federal Revenue Collections	Tax Year to Which Collections Relate			
		2008	2007	2006	Prior Years
Individual income and tax withholdings	2,294.3	1,455.0	799.2	23.5	16.6
Corporation income taxes	354.0	222.0	114.0	2.0	16.0
Unemployment taxes	39.5	21.9	10.1	7.4	0.1
Excise taxes	68.4	50.2	17.9	0.1	0.2
Estate and gift taxes	29.8	-	19.2	1.3	9.3
Railroad retirement taxes	4.9	3.7	1.2	-	-
Federal Reserve earnings	33.6	25.9	7.7	-	-
Fines, penalties, interest, and other revenue	6.6	6.1	0.4	0.1	-
Customs duties	28.6	28.6	-	-	-
Subtotal	2,859.7	1,813.4	969.7	34.4	42.2
Less: amounts collected for non-Federal entities	(0.9)				
Total	2,858.8				

Treasury is the Government's principal revenue-collecting agency. Collections of individual income tax and tax withholdings consist of Federal Insurance Contributions Act (FICA)/Self-Employment Contributions Act (SECA) and other taxes.

Federal Tax Refunds Disbursed for the Year Ended September 30, 2008

(In billions of dollars)	Refunds Disbursed	Tax Year to Which Refunds Relate			
		2008	2007	2006	Prior Years
Individual income and tax withholdings	369.3	0.9	342.1	19.2	7.1
Corporation income taxes	54.3	2.2	19.6	10.4	22.1
Unemployment taxes	0.1	-	0.1	-	-
Excise taxes	1.3	0.5	0.5	0.1	0.2
Estate and gift taxes	1.0	-	0.3	0.4	0.3
Customs duties	1.3	0.7	0.2	0.1	0.3
Total	427.3	4.3	362.8	30.2	30.0

Reconciliation of Revenue to Collections for the Year Ended September 30

(In billions of dollars)	2008	2007
Consolidated revenue per the Statements of Operations and Changes in Net Position	2,661.4	2,627.3
Tax refunds	427.3	299.7
Stimulus Act Recovery Rebate Payments	(94.3)	-
Earned income tax credit and child tax credit imputed revenue	(59.2)	(58.4)
Nontax-related fines and penalties reported by agencies	(40.7)	(33.8)
Nontax-related earned revenue	(35.7)	(29.7)
Collections of Federal revenue	2,858.8	2,805.1

Consolidated revenue in the Statements of Operations and Changes in Net Position is presented on a modified cash basis, is net of tax refunds, and includes other nontax related revenue. Stimulus Act Recovery Rebate payments, Earned Income Tax Credit, and Child Tax Credit amounts (unaudited) are included in gross cost in the Statements of Net Cost as a component of Treasury.

On the other hand, collections of Federal revenue are reported on a gross cash basis. The table above reconciles total revenue to collections.

Collections of Federal Revenue for the Year Ended September 30, 2007

(In billions of dollars)	Federal Revenue Collections	Tax Year to Which Collections Relate			
		2007	2006	2005	Prior Years
Individual income and tax withholdings	2,201.5	1,408.6	750.6	23.9	18.4
Corporation income taxes	395.3	253.4	116.3	2.9	22.7
Unemployment taxes	39.4	21.9	9.8	7.6	0.1
Excise taxes	69.9	51.8	17.8	0.1	0.2
Estate and gift taxes	27.0	-	16.2	1.6	9.2
Railroad retirement taxes	4.7	3.6	1.1	-	-
Federal Reserve earnings	32.0	26.2	5.8	-	-
Fines, penalties, interest, and other revenue	9.5	9.1	0.4	-	-
Customs duties	26.3	26.3	-	-	-
Subtotal	2,805.6	1,800.9	918.0	36.1	50.6
Less: amounts collected for non-Federal entities	(0.5)				
Total	2,805.1				

Federal Tax Refunds Disbursed for the Year Ended September 30, 2007

(In billions of dollars)	Refunds Disbursed	Tax Year to Which Refunds Relate			
		2007	2006	2005	Prior Years
Individual income and tax withholdings	261.1	1.8	235.2	17.8	6.3
Corporation income taxes	28.2	1.2	8.2	4.3	14.5
Unemployment taxes	0.1	-	0.1	-	-
Excise taxes	2.4	0.4	0.6	0.3	1.1
Estate and gift taxes	1.0	-	0.3	0.5	0.2
Customs duties	6.9	5.6	0.2	0.3	0.8
Total	299.7	9.0	244.6	23.2	22.9

Note 18. Prior Period Adjustments

Prior Period Adjustments for the Year Ended September 30

(In billions of dollars)	Changes to Net Position 2008	2007
Prior Period Adjustments		
Department of Agriculture	11.5	-
National Aeronautics and Space Administration	-	(12.7)
Other prior period adjustments	(0.1)	(1.2)
Total prior period adjustments	11.4	(13.9)

DHS deposits 30 percent of customs duties collected into an unavailable receipt account. USDA receives an amount annually from this account in accordance with 7 USC 612c to encourage exportation and domestic consumption of agricultural products. Treasury and OMB decided that Agriculture should be assigned responsibility for the unavailable receipt account to improve Governmentwide reporting. Consequently, the cumulative effect of this change on prior periods increased the beginning balance of Net Position by $13.6 billion. Additionally, USDA implemented a reclassification of its road prism assets from general plant, property, and equipment to Stewardship plant, property, and equipment. This change removes a net book value of $2.1 billion from the beginning balance of Net Position. The net value of these two numbers increased USDA's beginning balance of Net Position by $11.5 billion.

In fiscal year 2007, NASA recorded prior period adjustments for $12.7 billion (net decrease), primarily to reflect a change in accounting principle for property, plant, and equipment to reclassify costs previously categorized as general property, plant, and equipment to R&D expenses. After a detailed review of all items previously categorized as property, plant, and equipment, NASA concluded certain projects are more properly classified as R&D, and should not be classified, in their entirety, as capital assets under the classification of property, plant, and equipment. Accordingly, NASA applied the provisions of SFAS No. 2, Accounting for R&D Costs, to account for its R&D projects. NASA believes the recognition and measurement requirements of SFAS No. 2 result in reporting financial information that is more relevant and accurate.

Note 19. Contingencies

Financial Treatment of Loss Contingencies

Loss contingencies that are assessed to be at least reasonably possible are disclosed in this note. Loss contingencies involve situations where there is an uncertainty of a possible loss. The reporting of loss contingencies depends on the likelihood that a future event or events will confirm the loss or impairment of an asset or the incurrence of a liability. Terms used to assess the range for the likelihood of loss are probable, reasonably possible, and remote. Loss contingencies that are assessed as probable and measurable are accrued in the financial statements. Loss contingencies that are assessed as remote are not reported in the financial statements, nor disclosed in the notes. All other material loss contingencies are disclosed in this note. The following table provides criteria for how Federal agencies are to account for loss contingencies, based on the likelihood of the loss and measurability.[1]

Likelihood of future outflow or other sacrifice of resources.	**Loss amount can be reasonably measured.**	**Loss range can be reasonably measured.**	**Loss amount or range cannot be reasonably measured.**
Probable. Future confirming event(s) are more likely to occur than not.[2]	Accrue the liability. Reported on Balance Sheet and Statement of Net Cost.	Accrue liability using best estimate or minimum amount in loss range if there is no best estimate, and disclose nature of contingency and range of estimated liability.	Disclose nature of contingency and include a statement that an estimate cannot be made.
Reasonably possible. Possibility of future confirming event(s) occurring is more than remote and less than likely.	Disclose nature of contingency and estimated loss amount.	Disclose nature of contingency and estimated loss range.	Disclose nature of contingency and include a statement that an estimate cannot be made.
Remote. Possibility of future event(s) occurring is slight.	No disclosure.	No disclosure.	No disclosure.

[1] In addition, a third condition must be met to be a loss contingency: a past event or an exchange transaction must occur.

[2] For loss contingencies related to litigation, probable is defined as the future confirming event or events are more likely than not to occur, with the exception of pending or threatened litigation and unasserted claims. For the pending or threatened litigation and unasserted claims, the future confirming event or events are likely to occur.

The Government is subject to loss contingencies that include insurance and litigation cases. These loss contingencies arise in the normal course of operations and their ultimate disposition is unknown. Based on information currently available, however, it is management's opinion that the expected outcome of these matters, individually or in the aggregate, will not have a material adverse effect on the financial statements, except for the insurance and litigation described in the following sections:

Insurance Contingencies

At the time an insurance policy is issued, a contingency arises. The contingency is the risk of loss assumed by the insurer, that is, the risk of loss from events that may occur during the term of the policy. The Government has insurance contingencies that are reasonably possible in the amount of $64.0 billion as of September 30, 2008, and $67.8 billion as of September 30, 2007. The major programs are identified below:

- PBGC reported $46.8 billion and $65.7 billion as of September 30, 2008 and 2007, respectively, for the estimated aggregate unfunded vested benefits exposure to the PBGC for private-sector single-employer and multiemployer defined pension plans that is classified as a reasonably possible exposure to loss.
- FDIC reported $17.2 billion and $0.9 billion as of September 30, 2008 and 2007, respectively, for identified additional risk in the financial services industry that could result in additional loss to the Deposit Insurance Fund should potentially vulnerable insured institutions ultimately fail. Actual losses, if any, will largely depend on future economic and market conditions.

Insurance in Force

Insurance in Force is the accumulation of policy limits for all policies issued and outstanding at a point in time. The Government has Insurance in Force in the amount of $1,660.1 billion as of September 30, 2008, and $1,157.3 billion as of September 30, 2007. These amounts represent estimated maximum exposure to insurance claims and guarantee programs. The major programs are identified below:

- The Department of Homeland Security reported $1,600.0 billion and $1,100.0 billion as of September 30, 2008, and 2007, respectively, for the National Flood Insurance Program.
- The Export-Import Bank of the United States reported $39.9 billion and $39.1 billion as of September 30, 2008, and 2007, respectively, for Export Credit Insurance.

Deposit Insurance

Deposit insurance covers all types of deposit accounts such as checking, NOW and savings accounts, money market deposit accounts, and certificates of deposit (CDs) received at an insured bank, savings association, or credit union. The insurance covers the balance of each depositor's account, dollar-for-dollar, up to the insurance limit, including principal and any accrued interest through the date of the insured financial institution's closing. As a result, the Government has an aggregated insured deposit exposure estimated at approximately $5,063.7 billion as of September 30, 2008, and $4,800.2 billion as of September 30, 2007, which represent the total face amount of insurance in force. However, these amounts represent maximum possible losses assuming all the FDIC and NCUA member depository institutions were to fail (i.e., the likelihood of this occurring is remote) and the acquired assets provided no recovery of funds. Actual losses have generally been a very small fraction of the aggregate estimated insured deposits. The breakdown by agency is identified below:

- FDIC has estimated insured deposits of $4,462.0 billion as of September 30, 2008, and $4,239.0 billion as of September 30, 2007, for the Deposit Insurance Fund.
- NCUA has estimated insured deposits of $601.6 billion as of September 30, 2008, and $561.2 billion as of September 30, 2007, for the National Credit Union Share Insurance Fund.

Legal and Other Contingencies

Legal and other contingencies as of September 30, 2008, and 2007, are summarized in the table below:

(In billions of dollars)	Accrued Liabilities [1]	2008 Estimated Range of Loss for Certain Cases [2]		Accrued Liabilities [1]	2007 Estimated Range of Loss for Certain Cases [2]	
		Lower End	Upper End		Lower End	Upper End
Legal and other contingencies						
Probable............	6.6	5.8	7.8	6.4	6.4	8.0
Reasonably possible		8.0	21.4		3.6	6.6

[1] Accrued liabilities are recorded and presented in the related line items of the balance sheet.
[2] Does not reflect the total range of loss; many cases assessed as reasonably possible of an unfavorable outcome did not include estimated losses that could be determined.

The Government is party to various administrative claims and legal actions brought against it, some of which may ultimately result in settlements or decisions against the Government.

Management and legal counsel have determined that it is "probable" that some of these actions will result in a loss to the Government and the loss amounts are reasonably measurable. The estimated liabilities for these cases are $6.6 billion and $6.4 billion as of September 30, 2008, and 2007, respectively, and are reflected in the balance sheet as "Insurance Liabilities" or "Other Liabilities." A few of the major cases are summarized below:

- HHS has accrued $3.8 billion for contingent liabilities related to administrative proceedings, legal actions, and tort claims as of September 30, 2008. HHS Centers for Medicare and Medicaid Services has accrued $3.5 billion for Medicaid, which consists of Medicaid and audit and program disallowances of $0.7 billion and $2.8 billion for reimbursements of State Plan amendments. Contingent liabilities have been established as a result of Medicaid audit and program disallowances that are currently being appealed by the States. HHS will be required to pay these amounts if the appeals are decided in favor of the States.
- DOI has accrued $1.2 billion for contingent liabilities, consisting of numerous claims and lawsuits that are awaiting adjudication. These actions typically relate to administrative and judicial claims, contract related actions, tribal and Indian trust-related matters, personnel and employment related matters, and various land and resource related claims and adjudications.

There are also administrative claims and legal actions pending where adverse decisions are considered by management and legal counsel as "reasonably possible" with an estimate of potential loss or a range of potential loss. The estimated potential losses for such claims and actions range from $8.0 billion to $21.4 billion as of September 30, 2008, and from $3.6 billion to $6.6 billion as of September 30, 2007. Two of the major cases are summarized below:

- DHS has received and has pending administrative claims and 30 Class Action lawsuits. The claims and lawsuits are related to claims against FEMA for personal injuries allegedly resulting from exposure to formaldehyde in temporary housing units; i.e., travel trailers, and mobile homes, issued by FEMA in response to Hurricanes Katrina and Rita.
- USDA has pending class action discrimination suits.

Numerous litigation cases are pending where the outcome is uncertain or it is reasonably possible that a loss has been incurred and where estimates cannot be made. There are other litigation cases where the plaintiffs have not made claims for specific dollar amounts, but the claimed amounts may be significant. The ultimate resolution of these legal actions for which the potential loss could not be determined may materially affect the U.S. Government's financial position or operating results. Examples of specific cases are summarized below:

- Native Americans allege that DOI and Treasury have breached trust obligations with respect to the management of the plaintiffs' individual Indian monies. The plaintiffs have not made claims for specific dollar amounts in the Federal district court proceedings, but in public statements have asserted that the class is owed tens of billions of dollars.
- DOI is involved in two related cases in connection with Indian mineral lease amendments containing increased royalty rates negotiated by the Navajo Nation and the Hopi Tribe. The tribes assert that the United States breached fiduciary duties to the tribes when the Secretary approved the tribally-negotiated amendments.
- Threatened or pending DOD litigation cases include claims asserted under the Federal Tort Claims Act (FTCA), patent infringement and damage claims, and contract litigation involving cost accounting standards.
- Numerous complaints have arisen as a result of Hurricane Katrina. These New Orleans FTCA cases allege personal injury, wrongful death, and property damages as a result of massive flooding caused by the hurricane. There are over 507,000 administrative claims filed in relation to Hurricane Katrina and 1,000 related suits in Federal district courts. Additional suits are expected.

Environmental and Disposal Contingencies

Environmental and disposal contingencies as of September 30, 2008, and 2007, are summarized in the table below:

(In billions of dollars)	2008 Accrued Liabilities [1]	2008 Estimated Range of Loss for Certain Cases [2]		2007 Accrued Liabilities [1]	2007 Estimated Range of Loss for Certain Cases [2]	
		Lower End	Upper End		Lower End	Upper End
Environmental and disposal contingencies						
Probable	12.7	12.7	13.0	11.2	11.2	11.3
Reasonably possible		0.4	0.4		0.3	0.8

[1] Accrued liabilities are recorded and presented in the related line items of the balance sheet.
[2] Does not reflect the total range of loss; many cases assessed as reasonably possible of an unfavorable outcome did not include estimated losses that could be determined.

The Government is subject to loss contingencies for a variety of environmental cleanup costs for the storage and disposal of hazardous material and the operations and closures of facilities at which environmental contamination may be present.

Management and legal counsel have determined that it is "probable" that some of these actions will result in a loss to the Government and the loss amounts are reasonably measurable. The estimated liabilities for these cases are $12.7 billion and $11.2 billion as of September 30, 2008, and 2007, respectively, and are reflected on the balance sheet as "Other Liabilities." DOE is subject to Spent Nuclear Fuel litigation for damages suffered by all utilities as a result of the delay in beginning disposal of spent nuclear fuel and also damages for alleged exposures to radioactive and/or toxic substances. Significant claims for partial breach of contract and a large number of class action and/or multiple plaintiff tort suits have been filed with estimated liability amounts of $12.4 billion and $11.1 billion as of September 30, 2008, and 2007, respectively.

Other Contingencies

DOT reported the following other contingencies:

- The Federal Highway Administration (FHWA) reimburses states for construction costs on projects related to the Federal Highway System of roads. FHWA has pre-authorized $46.2 billion to the states to establish budgets for its construction projects for fiscal years ending September 30, 2008, and 2007. Congress has not provided appropriations for these projects and no liability is accrued in the consolidated financial statements.
- The Federal Transit Administration (FTA) provides grants to state and local transit authorities and agencies. FTA executes Full Funding Grant Agreements authorizing transit authorities to establish project budgets and incur costs with their own funds in advance of annual appropriations by Congress. Under these agreements, FTA has committed approximately $1.7 billion and $3.9 billion for fiscal years ending September 30, 2008, and 2007. Congress has not provided appropriations for these commitments and no liability is reflected in the consolidated financial statements.

Note 20. Commitments

Long-Term Operating Leases as of September 30

(In billions of dollars)	2008	2007
General Services Administration	23.9	23.1
U.S. Postal Service	8.3	8.4
Department of Justice	4.3	3.1
Department of Homeland Security	2.3	0.9
Department of Health and Human Services	1.5	1.6
Department of State	1.0	1.8
Department of Agriculture	0.8	0.8
Other operating leases	4.6	4.8
Total long-term operating leases	46.7	44.5

The Government has entered into contractual commitments that require future use of financial resources. It has significant amounts of long-term lease obligations and undelivered orders. Undelivered orders represent the value of goods and services ordered that have not yet been received.

The Government has other contractual commitments that may require future use of financial resources. For example, the Government has callable subscriptions in the Multilateral Development Banks (MDBs), which are autonomous international financial entities that finance economic and social development projects in developing countries. Callable capital resembles promissory notes to honor MDB debts if the MDB cannot otherwise meet its obligations through its other available resources. MDBs are able to use callable capital as backing to obtain very favorable financing terms when borrowing from world capital markets. Treasury officials do not anticipate any calls on MDB subscriptions. To date, there has never been a call on this capital for any of the major MDBs.

Undelivered Orders and Other Commitments as of September 30

(In billions of dollars)	2008	2007
Undelivered Orders:		
Department of Defense	316.1	246.0
EOP Foreign Military Sales Program	77.6	63.8
Department of Transportation	71.7	72.2
Department of Health and Human Services	69.3	72.1
Department of the Treasury	57.1	55.8
Department of Housing and Urban Development	56.8	65.2
Department of Education	47.2	48.2
Department of Agriculture	37.8	34.9
Department of Homeland Security	33.6	29.9
Department of Energy	13.6	12.2
Department of State	13.6	11.3
Agency for International Development	11.6	12.0
Department of Justice	8.9	9.0
National Science Foundation	8.0	7.7
Environmental Protection Agency	7.8	8.0
Department of Veterans Affairs	7.4	4.6
All other agencies	32.0	32.2
Total undelivered orders	870.1	785.1
Other Commitments:		
Senior GSE Preferred Stock Purchase Agreement	186.2	-
Callable capital subscriptions for multilateral development banks	62.3	62.2
Sales of surplus power	32.8	21.2
Power purchase obligations	7.2	4.8
Long-term satellite and systems	4.8	7.7
Fuel purchase obligations	4.2	3.1
Agriculture direct loans and guarantees	3.8	2.7
Contract Options and Negotiations	3.7	-
All other commitments	4.7	8.1
Total other commitments	309.7	109.8

Other Commitments and Risks

The U.S. Government is a party to major treaties and other international agreements. These treaties and other international agreements address various issues including, but not limited to, trade, commerce, security, and arms that may involve financial obligations or give rise to possible exposure to losses. A comprehensive analysis to determine any such financial obligations or possible exposure to loss and their related effect on the consolidated financial statements of the U.S. Government has not yet been performed.

On September 7, 2008, the Secretary of the Treasury announced a program designed to protect the U.S. markets and the taxpayers from the systemic risk posed by the financial condition of the GSE. Treasury entered into a senior preferred stock purchase contract with Freddie Mac and Fannie Mae. They are indefinite in duration and have a capacity of $100 billion each, an amount chosen to demonstrate a strong commitment to the GSE creditors and mortgage-backed security holders. Treasury also established a new secured lending credit facility which will be available to Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. Funding will be provided directly by Treasury from its general fund held at the FRBNY in exchange for eligible collateral from the GSE which will be limited to guaranteed mortgage-backed securities issued by the GSE. See Note 8 for further information.

In addition, the U. S. Government has entered into other agreements that could potentially require claims on Government resources in the future. Examples include war risk and terrorism risk insurance.

Note 21. Earmarked Funds

Earmarked Funds as of September 30, 2008 [1]

(In billions of dollars)	Federal Old-Age and Survivors Insurance Trust Fund	Military Retirement Fund	Civil Service Retirement and Disability Fund	Medicare-Eligible Retiree Health Care Fund (MERHCF)	Federal Hospital Insurance Trust Fund (Medicare Part A)	Civil Service Health Benefits Program Trust Funds
Assets:						
Cash and other monetary assets	-	-	-	-	-	-
Fund balance with Treasury	(0.3)	-	-	-	0.2	0.9
Investments in U.S. Treasury securities	2,150.7	250.3	728.9	132.8	318.7	47.8
Other Federal assets	26.4	2.7	10.1	1.5	26.8	1.1
Non-Federal assets	2.5	-	0.3	-	1.1	0.9
Total assets	2,179.3	253.0	739.3	134.3	346.8	50.7
Liabilities:						
Liabilities due and payable to beneficiaries	46.4	3.4	5.0	0.6	21.0	4.1
Other Federal liabilities	4.2	-	0.1	0.1	22.5	0.3
Other non-Federal liabilities	-	1,150.7	1,387.8	500.3	0.4	331.8
Total liabilities	50.6	1,154.1	1,392.9	501.0	43.9	336.2
Total net position	2,128.7	(901.1)	(653.6)	(366.7)	302.9	(285.5)
Total liabilities and net position	2,179.3	253.0	739.3	134.3	346.8	50.7
Change in net position:						
Beginning net position	1,946.7	(810.6)	(613.6)	(407.9)	295.0	(262.8)
Prior period adjustment	-	-	-	-	-	-
Beginning net position, adjusted	1,946.7	(810.6)	(613.6)	(407.9)	295.0	(262.8)
Investment revenue	104.1	15.5	37.3	8.2	16.6	1.9
Individual income taxes	573.8	-	-	-	197.2	-
Unemployment and excise taxes	-	-	-	-	-	-
Other taxes and receipts	-	-	-	-	0.6	-
Miscellaneous earned revenues	-	-	-	-	-	-
Other changes in fund balance (e.g., appropriations, transfers)	10.0	65.1	30.9	24.4	11.2	8.7
Non-program expenses	-	-	-	-	-	-
Program net cost	505.9	171.1	108.2	(8.6)	217.7	33.3
Ending net position	2,128.7	(901.1)	(653.6)	(366.7)	302.9	(285.5)

[1] By law, certain expenses (costs), revenues, and other financing sources related to the administration of the above funds are not charged to the funds and are therefore financed and/or credited to other sources.

Earmarked Funds as of September 30, 2008 [1]

(In billions of dollars)	Federal Disability Insurance Trust Fund	Unemployment Trust Fund	Federal Supplementary Medical Insurance Trust Fund (Medicare Parts B and D)	All Other Earmarked Funds	Intra-Earmarked Fund Eliminations	Total Earmarked Funds
Assets:						
Cash and other monetary assets	-	-	0.3	22.3	-	22.6
Fund balance with Treasury	(0.4)	(0.1)	12.3	77.5	-	90.1
Investments in U.S. Treasury securities	216.5	72.4	59.1	177.6	-	4,154.8
Other Federal assets	2.7	1.2	26.5	18.3	(53.5)	63.8
Non-Federal assets	3.0	1.5	5.0	116.2	-	130.5
Total assets	221.8	75.0	103.2	411.9	(53.5)	4,461.8
Liabilities:						
Liabilities due and payable to beneficiaries	24.1	1.6	24.0	2.0	-	132.2
Other Federal liabilities	1.0	1.3	26.9	61.9	(53.5)	64.8
Other non-Federal liabilities	-	-	0.3	188.9	-	3,560.2
Total liabilities	25.1	2.9	51.2	252.8	(53.5)	3,757.2
Total net position	196.7	72.1	52.0	159.1	-	704.6
Total liabilities and net position	221.8	75.0	103.2	411.9	(53.5)	4,461.8
Change in net position:						
Beginning net position	193.9	75.0	43.9	160.6	-	620.2
Prior period adjustment	-	-	-	-	-	-
Beginning net position, adjusted	193.9	75.0	43.9	160.6	-	620.2
Investment revenue	11.0	3.6	2.5	0.3	-	201.0
Individual income taxes	97.4	-	-	-	-	868.4
Unemployment and excise taxes	-	39.4	-	51.8	-	91.2
Other taxes and receipts	0.1	-	3.3	30.7	(0.4)	34.3
Miscellaneous earned revenues	-	-	-	5.8	-	5.8
Other changes in fund balance (e.g., appropriations, transfers)	(1.5)	(3.7)	179.6	13.3	-	338.0
Non-program expenses	-	-	-	1.9	-	1.9
Program net cost	104.2	42.2	177.3	101.5	(0.4)	1,452.4
Ending net position	196.7	72.1	52.0	159.1	-	704.6

[1] By law, certain expenses (costs), revenues, and other financing sources related to the administration of the above funds are not charged to the funds and are therefore financed and/or credited to other sources.

Earmarked Funds as of September 30, 2007[1] (Restated)

(In billions of dollars)	Federal Old-Age and Survivors Insurance Trust Fund	Military Retirement Fund	Civil Service Retirement and Disability Fund	Medicare-Eligible Retiree Health Care Fund (MERHCF)	Federal Hospital Insurance Trust Fund (Medicare Part A)	Civil Service Health Benefits Program Trust Funds
Assets:						
Cash and other monetary assets	-	-	-	-	-	-
Fund balance with Treasury	(0.9)	-	-	-	-	0.9
Investments in U.S. Treasury Securities	1,968.3	215.4	701.7	108.4	319.4	41.3
Other Federal assets	25.0	2.8	9.8	1.1	25.4	0.9
Non-Federal assets	2.3	-	0.3	-	1.0	0.7
Total assets	1,994.7	218.2	711.8	109.5	345.8	43.8
Liabilities and net position:						
Liabilities due and payable to beneficiaries	44.1	3.5	4.8	0.6	19.4	3.8
Other Federal liabilities	3.9	-	0.1	0.1	29.5	0.3
Other non-Federal liabilities	-	1,025.3	1,320.5	516.7	1.9	302.5
Total liabilities	48.0	1,028.8	1,325.4	517.4	50.8	306.6
Total net position	1,946.7	(810.6)	(613.6)	(407.9)	295.0	(262.8)
Total liabilities and net position	1,994.7	218.2	711.8	109.5	345.8	43.8
Change in net position:						
Beginning net position	1,771.9	(758.7)	(591.6)	(453.5)	287.9	(273.5)
Prior period adjustment	(5.0)	-	-	-	-	-
Beginning net position, adjusted	1,766.9	(758.7)	(591.6)	(453.5)	287.9	(273.5)
Investment revenue	97.4	10.3	37.2	4.4	16.3	1.0
Individual income taxes	553.4	-	-	-	188.0	-
Unemployment and excise taxes	-	-	-	-	-	-
Other taxes and receipts	-	-	-	-	-	-
Miscellaneous earned revenue	-	-	-	-	-	-
Other changes in fund balance (e.g., appropriations, transfers)	10.6	43.1	13.8	27.3	11.4	25.6
Non-program expenses	-	-	-	-	-	-
Program net cost	481.6	105.3	73.0	(13.9)	208.6	15.9
Ending net position	1,946.7	(810.6)	(613.6)	(407.9)	295.0	(262.8)

[1] By law, certain expenses (costs), revenues, and other financing sources related to the administration of the above funds are not charged to the funds and are therefore financed and/or credited to other sources.

Earmarked Funds as of September 30, 2007[1] (Restated)

(In billions of dollars)	Federal Disability Insurance Trust Fund	Unemployment Trust Fund	Federal Supplementary Medical Insurance Trust Fund (Medicare Parts B and D)	All Other Earmarked Funds	Intra-Earmarked Fund Eliminations	Total Earmarked Funds
Assets:						
Cash and other monetary assets	-	-	0.1	21.8	-	21.9
Fund balance with Treasury	(0.4)	0.1	8.8	70.7	-	79.2
Investments in U.S. Treasury Securities	213.8	74.9	39.2	169.4	-	3,851.8
Other Federal assets	2.7	1.2	32.9	17.4	(58.3)	60.9
Non-Federal assets	2.8	1.5	10.8	93.5	-	112.9
Total assets	218.9	77.7	91.8	372.8	(58.3)	4,126.7
Liabilities and net position:						
Liabilities due and payable to beneficiaries	21.7	1.3	22.2	2.0	-	123.4
Other Federal liabilities	1.0	1.4	24.8	62.0	(58.3)	64.8
Other non-Federal liabilities	2.3	-	0.9	148.2	-	3,318.3
Total liabilities	25.0	2.7	47.9	212.2	(58.3)	3,506.5
Total net position	193.9	75.0	43.9	160.6	-	620.2
Total liabilities and net position	218.9	77.7	91.8	372.8	(58.3)	4,126.7
Change in net position:						
Beginning net position	183.0	66.4	41.6	150.8	-	424.3
Prior period adjustment	5.0	-	0.1	1.0	-	1.1
Beginning net position, adjusted	188.0	66.4	41.7	151.8	-	425.4
Investment revenue	11.0	3.3	2.1	9.7	-	192.7
Individual income taxes	94.0	-	-	-	-	835.4
Unemployment and excise taxes	-	39.3	-	53.6	-	92.9
Other taxes and receipts	0.1	1.6	-	34.0	(0.5)	35.2
Miscellaneous earned revenue	-	-	-	4.4	-	4.4
Other changes in fund balance (e.g., appropriations, transfers)	(1.6)	(3.5)	159.0	4.9	-	290.6
Non-program expenses	-	-	-	3.0	-	3.0
Program net cost	97.6	32.1	158.9	94.8	(0.5)	1,253.4
Ending net position	193.9	75.0	43.9	160.6	-	620.2

[1] By law, certain expenses (costs), revenues, and other financing sources related to the administration of the above funds are not charged to the funds and are therefore financed and/or credited to other sources.

Earmarked funds are financed by specifically identified revenues, often supplemented by other financing sources, which remain available over time. These specifically identified revenues and other financing sources are required by statute to be used for designated activities, benefits, or purposes and must be accounted for separately from the Government's general revenues. Earmarked funds generally include trust funds, public enterprise revolving funds (not including credit reform financing funds) and special funds.

In the Federal budget, the term "trust fund" means only that the law requires a particular fund be accounted for separately, used only for a specified purpose, and designated as a trust fund. A change in law may change the future receipts and the terms under which the fund's resources are spent. In the private sector, trust fund refers to funds of one party held and managed by a second party (the trustee) in a fiduciary capacity. The activity of earmarked funds differs from fiduciary activities primarily in that earmarked fund assets are Government-owned.

Public enterprise revolving funds include expenditure accounts authorized by law to be credited with offsetting collections, mostly from the public, that are generated by and earmarked to finance a continuing cycle of business-type operations. Some of the financing for these funds may be from appropriations.

Special funds are Federal funds earmarked by law for a specific purpose. Special funds include the special fund receipt account and the special fund expenditure account.

The tables above depict major earmarked funds chosen based on their significant financial activity and importance to taxpayers. All other Government earmarked funds not shown separately are aggregated as "all other."

Total assets represent the unexpended balance from all sources of receipts and amounts due to the earmarked funds, regardless of source, including related Governmental transactions. These are transactions between two different entities within the Government (for example, monies received by one entity of the Government from another entity of the Government).

The intragovernmental assets are comprised of fund balances with Treasury, investments in Treasury securities – including unamortized amounts, and other assets that include the related accrued interest receivable on Federal investments. These amounts were eliminated in preparing the principal financial statements.

The non-Federal assets represent only the activity with individuals and organizations outside of the Government.

Most of the earmarked fund assets are invested in intragovernmental debt holdings. The Government does not set aside assets to pay future benefits or other expenditures associated with earmarked funds. The cash receipts collected from the public for an earmarked fund are deposited in the U.S. Treasury, which uses the cash for general Government purposes. Treasury securities are issued to Federal agencies as evidence of its receipts. Treasury securities are an asset to the Federal agencies and a liability to the U.S. Treasury and, therefore, they do not represent an asset or a liability in the *Financial Report of the U.S. Government*. These securities require redemption if a fund's disbursements exceeds its receipts. Redeeming these securities will increase the Government's financing needs and require more borrowing from the public (or less repayment of debt), or will result in higher taxes than otherwise would have been needed, or less spending on other programs than otherwise would have occurred, or some combination thereof. See Note 11—Federal Debt Securities Held by the Public and Accrued Interest for further information related to the investments in Federal debt securities.

Depicted below is a description of the major earmarked funds shown in the above tables, which also includes the names of the Government agencies that administer each particular fund. For detailed information regarding these earmarked funds, please refer to the financial statements of the corresponding administering agencies. For information on the benefits due and payable liability associated with certain earmarked funds, see Note 14—Benefits Due and Payable.

Federal Old-Age and Survivors Insurance Trust Fund

The Federal Old-Age and Survivors Insurance Trust Fund, administered by the Social Security Administration (SSA), provides a basic annuity to workers to protect them from loss of income at retirement and provide a guaranteed income to survivors in the event of the death of a family's primary wage earner.

Payroll and self-employment taxes primarily fund the Federal Old-Age and Survivors Insurance Trust Fund. Interest earnings on Treasury securities, Federal agencies' payments for the Social Security benefits earned by military and Federal civilian employees, and Treasury payments for a portion of income taxes collected on Social Security benefits provide the fund with additional income. The law establishing the Federal Old-Age and Survivors Insurance Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 42 U.S.C. § 401.

Military Retirement Fund

The Military Retirement Fund, administered by DOD, provides retirement benefits for Army, Navy, Marine Corps, and Air Force personnel and their survivors. The fund is financed by DOD contributions, appropriations, and interest earnings on Treasury securities. The laws establishing the Military Retirement Fund and authorizing the depositing of amounts to the credit of the trust fund are set forth in 10 U.S.C. § 1461-1467.

Civil Service Retirement and Disability Fund

The Civil Service Retirement and Disability Fund (CSRDF) covers two Federal civilian retirement systems: the Civil Service Retirement System (CSRS)—for employees hired before 1984, and the Federal Employees' Retirement System (FERS)—for employees hired after 1983. OPM administers the CSRS and the FERS systems. The laws establishing the CSRDF and authorizing the depositing of amounts to the credit of the trust fund are set forth in 5 U.S.C. § 8334-8348. Funding sources include:

- Federal civilian employees' contributions.
- Agencies' contributions on behalf of employees.
- Appropriations.
- Interest earnings on Treasury securities.

Medicare-Eligible Retiree Health Care Fund

The Medicare-Eligible Retiree Health Care Fund, administered by DOD and established by 10 U.S.C. § 1111, finances and pays the liabilities under the DOD retiree health care programs for Medicare-eligible beneficiaries. Such beneficiaries include qualifying members, former members, and dependents of the Uniformed Services. The assets of the fund are comprised of any amounts appropriated to the trust fund, payments to the fund authorized by 10 U.S.C. § 1116, and interest earned on investments authorized by 10 U.S.C. § 1117.

Federal Hospital Insurance Trust Fund (Medicare Part A)

The Federal Hospital Insurance Trust Fund, administered by HHS, finances the Hospital Insurance Program (Medicare Part A). This program funds the cost of inpatient hospital and related care for individuals age 65 or older who meet certain insured status requirements, and eligible disabled people.

The Federal Hospital Insurance Trust Fund is financed primarily by payroll taxes, including those paid by Federal agencies. It also receives income from interest earnings on Treasury securities and a portion of income taxes collected on Social Security benefits. The law establishing the Federal Hospital Insurance Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 42 U.S.C. § 1395i.

Civil Service Health Benefits Program Trust Funds

The Civil Service Health Benefits Program (HBP) provides health benefits to Federal employees and dependents as well as to Federal retirees, including USPS retirees, and survivor annuitants. The program is operated through two revolving trust funds. The HBP administers a wide variety of health and wellness plans including Fee-For-Service and Health Maintenance Organization plans. Retired employees can choose to continue coverage upon separation from the Government. OPM administers the HBP.

The law establishing the first HBP trust fund, the Federal Employees Health Benefits (FEHB) Fund, and authorizing the depositing of amounts to the credit of the trust fund is set forth in 5 U.S.C. § 8909. The FEHB fund is funded on a "pay-as-you-go" basis and funding sources include:

- Federal civilian employees' contributions.
- Agencies' contributions on behalf of employees.
- Appropriations (for "employer" share related to retirement program annuitants).
- Interest earnings on Treasury securities.

The *Postal Accountability and Enhancement Act of 2006* (Postal Act of 2006) (P.L. No 109-435, Title VIII), made significant changes in the funding of retiree health benefits for employees of the USPS, including the requirement for the USPS to make scheduled payments to the second HBP trust fund, the newly created Postal Service Retiree Health Benefits (PSRHB) Fund.

The laws establishing the PSRHB Fund and authorizing the depositing of amounts to the credit of the trust fund are set forth in 5 U.S.C. § 8909a. The Postal Act of 2006 requires the USPS to make scheduled payment contributions to the PSRHB Fund ranging from $5.4 billion to $5.8 billion per year from fiscal year 2007 through fiscal year 2016. Thereafter, the USPS will make annual payments in the amount of the normal cost payment. The PSRHB Fund is also funded by interest earnings on Treasury securities.

Federal Disability Insurance Trust Fund

The Federal Disability Insurance Trust Fund provides financial assistance and protection against the loss of earnings due to a wage earner's disability. The SSA administers this Trust Fund.

Like the Federal Old-Age and Survivors Insurance Trust Fund, payroll taxes primarily fund the Federal Disability Insurance Trust Fund. The fund also receives income from interest earnings on Treasury securities, Federal agencies' payments for the Social Security benefits earned by military and Federal civilian employees, and a portion of income taxes collected on Social Security benefits. The law establishing the Federal Disability Insurance Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 42 U.S.C. § 401.

Unemployment Trust Fund

The Unemployment Trust Fund (UTF) provides temporary assistance to workers who lose their jobs. The program is administered through a unique system of Federal and State partnerships, established in Federal law, but executed through conforming State laws by State officials. DOL administers the Federal operations of the program.

Employer taxes provide the primary funding source for the UTF and constitute all the earmarked unemployment tax revenues as shown on the consolidated Statement of Operations and Changes in Net Position. For the years ending September 30, 2008, and 2007, UTF unemployment tax revenues were $39.4 billion and $39.3 billion, respectively. However, interest earnings on Treasury securities also provide income to the fund. Appropriations have supplemented the fund's income during periods of high and extended unemployment. The law establishing the UTF and authorizing the depositing of amounts to the credit of the trust fund is set forth in 42 U.S.C. § 1104.

Federal Supplementary Medical Insurance Trust Fund (Medicare Parts B and D)

The Federal Supplementary Medical Insurance Trust Fund, administered by HHS, finances the Supplementary Medical Insurance Program (Medicare Part B) and the Medicare Prescription Drug Benefit Program (Medicare Part D). These programs provide supplementary medical insurance for enrolled eligible participants to cover physician and outpatient services not covered by Medicare Part A and to obtain qualified prescription drug coverage, respectively. Medicare Part B financing is not based on payroll taxes; it is based on monthly premiums, income from the General Fund of the Treasury, and interest earnings on Treasury securities. The law establishing the Federal Supplementary Medical Insurance Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 42 U.S.C. § 1395t.

Medicare Part D was created by the *Medicare Prescription Drug, Improvement, and Modernization Act of 2003* (P.L. No. 108-173). Medicare Part D financing is similar to Part B; it is based on monthly premiums and income from the General Fund of the Treasury, not on payroll taxes. The law creating the Medicare prescription drug account within the Federal Supplementary Medical Insurance Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 42 U.S.C. § 1395w-116.

All Other Earmarked Funds

The Government is responsible for the management of numerous earmarked funds that serve a wide variety of purposes. The earmarked funds presented on an individual basis in the table above represent the majority of the Government's net position attributable to earmarked funds. All other earmarked activity is aggregated in accordance with SFFAS No. 27. For the years ending September 30, 2008 and 2007, there were approximately 537 and 521 earmarked funds, respectively. The earmarked funds within the "all other" aggregate, along with the agencies that administer them, include the following:

- Exchange Stabilization Fund—administered by Treasury.
- Railroad Retirement Trust Fund—administered by RRB.
- Universal Service Fund—administered by FCC.
- Federal Crop Insurance Corporation Fund and Funds for Strengthening Markets, Income, and Supply—administered by USDA.
- Superfund (Hazardous Substance) and Leaking Underground Storage Tanks—administered by EPA.
- U.S. Patent and Trademark Office—administered by DOC.
- Land and Water Conservation Fund, Historical Preservation Fund and Reclamation Fund—administered by DOI.
- Medical Care—administered by VA.
- Customs User Fees, Immigration Examination Fees and the National Flood Insurance Program—administered by DHS.
- Government National Mortgage Association (Ginnie Mae)—administered by HUD.

Excise Taxes

In addition, there are 10 other earmarked funds within the "all other" aggregate that contribute to all of the earmarked excise tax revenue shown on the consolidated Statement of Operations and Changes in Net Position. Two of these earmarked funds, the Highway Trust Fund and the Airport and Airway Trust Fund, provide more than 90 percent of the total earmarked excise tax revenues. Both of these earmarked funds are administered by the DOT and, for more detailed information regarding them, please refer to DOT's financial statements.

The Highway Trust Fund was established to promote domestic interstate transportation and to move people and goods. The fund provides Federal grants to States for highway construction, certain transit programs, and related transportation purposes. The law establishing the Highway Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 26 U.S.C. § 9503. Funding sources include earmarked excise taxes on gasoline and other fuels, certain tires, the initial sale of heavy trucks, and highway use by commercial motor vehicles. For the years ending September 30, 2008, and 2007, Highway Trust Fund excise tax revenues were $36.4 billion and $39.2 billion, respectively. As funds are needed for payments, the Highway Trust Fund Corpus investments are liquidated and funds are transferred to the Federal Highway Administration, the Federal Transit Administration, or other DOT entity, for payment of obligations.

The Airport and Airway Trust Fund provides for airport improvement and airport facilities maintenance. It also funds airport equipment, research, and a portion of the Federal Aviation Administration's administrative operational support. The law establishing the Airport and Airway Trust Fund and authorizing the depositing of amounts to the credit of the trust fund is set forth in 26 U.S.C. § 9502. Funding sources include:

- Taxes received from transportation of persons and property in the air and fuel used in commercial and general aviation.
- International departure taxes.
- Interest earnings on Treasury securities.

For the years ending September 30, 2008, and 2007, Airport and Airway Trust Fund excise tax revenues were $11.8 billion and $12.4 billion, respectively. These revenue amounts do not reflect any transfers from the Highway Trust Fund to the Airport and Airway Trust Fund for fuel which was used in aviation, but which was taxed at highway rates under P.L. 109-59 (SAFETEA-LU).

Intra-Earmarked Fund Eliminations

The intra-earmarked fund eliminations represent the activity between earmarked funds that are administered by different Federal agencies and which are eliminated to produce consolidated earmarked revenues and net costs as shown on the Statement of Operations and Changes in Net Position. Significant examples of such intra-earmarked fund activity include the financial interchanges and transactions between the Railroad Retirement Trust Fund, the Social Security Trust Funds, and the Medicare Trust Funds, which are administered by the Railroad Retirement Board (RRB), SSA and HHS, respectively. The financial interchanges and transactions between RRB's Railroad Retirement Trust Fund, SSA's Federal Old-Age and Survivors Insurance Trust Fund and the Disability Insurance Trust Fund, and HHS' Federal Hospital Insurance Trust Fund are intended to put the latter three trust funds in the same position they would have been had railroad employment been covered under the Social Security Act. For further information, see the Railroad Retirement program description within Note 23—Social Insurance.

Restatements

The Balance Sheet and Statement of Operations and Changes in Net Position as of September 30, 2007, were restated for the changes discussed below.

Due to a correction during the current year in the computation of the fiscal year 2007 asset and liability elimination amount, the previously reported asset and liability elimination amount was increased by $4.4 billion, thereby decreasing the previously reported amounts for total assets, total liabilities, and total liabilities and net position by $4.4 billion. In addition, as of September 30, 2007, there was one Federal Agency that, in fiscal year 2008, restated some of its fiscal year 2007 balances and transactions from non-earmarked funds to earmarked funds. This resulted in an increase in beginning and ending net position attributable to earmarked funds of $5.1 billion and $6.1 billion, respectively. This Federal Agency also had $1.0 billion of exchange revenues in excess of gross cost, resulting in a $1 billion decrease in total program net cost attributable to earmarked funds. As a result of this restatement, the previously reported amounts for total assets and for total liabilities and net position increased by $6.1 billion.

As of September 30, 2007, $4.4 billion of Other Taxes and Receipts for All Other Earmarked Funds were restated to Miscellaneous Earned Revenues to correct their presentation. These amounts relate to royalties retained by various earmarked funds within DOI.

In addition, various other restatements were made to certain line items to correct their presentation. As of September 30, 2007, the following restatements were made:

- Individual income and payroll taxes and net intragovernmental transfers were decreased and increased, respectively, by $11.8 billion to correct the amount of FICA/SECA taxes collected in fiscal year 2007 by HHS' Hospital Insurance Trust Fund.
- Excise taxes increased by $1.4 billion to correct their being included erroneously in other taxes and receipts.
- Other taxes and receipts increased by a net $13.5 billion. The increase was primarily due to $7.4 billion, $5.4 billion and $5.2 billion that had been erroneously included in program net cost, net intragovernmental transfers, and non-program expenses, respectively.
- Intragovernmental transfers decreased by a net $37.0 billion, primarily due to $42.1 billion of exchange revenue that should have been included in program net cost.

September 30, 2007 Restatements

(In billions of dollars)

Note Line Item	As Published	Agency Restatement	Change in Eliminations	All Other Changes	Total
Assets and Liabilities:					
Fund Balance with Treasury	73.3	5.9	-	-	79.2
Other Federal Assets	65.3	-	(4.4)	-	60.9
Other Non-Federal Assets	112.7	0.2	-	-	112.9
Total Assets	4,125.0	6.1	(4.4)	-	4,126.7
Other Federal Liabilities	69.2	-	(4.4)	-	64.8
Total Liabilities	3,510.9	-	(4.4)	-	3,506.5
Net Position	614.1	6.1	-	-	620.2
Total Liabilities and Net Position	4,125.0	6.1	(4.4)	-	4,126.7
Changes in Net Position:					
Beginning Net Position	419.2	5.1	-	-	424.3
Beginning Net Position, Adjusted	420.3	5.1	-	-	425.4
Individual Income Taxes*	847.2	-	-	(11.8)	835.4
Unemployment and Excise Taxes*	91.5	-	-	1.4	92.9
Other Taxes and Receipts*	21.7	-	-	13.5	35.2
Miscellaneous Earned Revenue	-	-	-	4.4	4.4
Other Changes in Fund Balance	327.6	-	-	(37.0)	290.6
Non-Program Expenses	(2.2)	-	-	5.2	3.0
Program Net Cost	1,289.1	(1.0)	-	(34.7)	1,253.4
Ending Net Position	614.1	6.1	-	-	620.2

* These line items were collectively labeled “Revenue from the public” in the published fiscal year 2007 earmarked funds note disclosure. However, these line items were individually published, as shown, in the fiscal year 2007 Statement of Operations and Changes in Net Position.

The restatements related to Changes in Net Position also affected the same line items in the Statement of Operations and Changes in Net Position by the same amounts. In addition, on the Balance Sheet, the previously reported amounts for net position – non-earmarked funds and for net position – earmarked funds decreased and increased, respectively, by $6.1 billion.

These restatements, including the restatements related to the above Federal Agency restatement and to miscellaneous earned revenues, did not affect total Governmentwide consolidated revenues and expenses or consolidated ending net position for the year ended September 30, 2007.

Note 22. Indian Trust Funds

U.S. Government as Trustee for Indian Trust Funds Held for Indian Tribes and Other Special Trust Funds – Cash Basis
Statement of Assets and Trust Fund Balances as of September 30

(In millions of dollars)	2008	2007
Assets:		
Cash and cash equivalents	519.4	602.5
Investments	2,483.8	2,278.2
Total Assets	3,003.2	2,880.7
Trust fund balances, held for Indian Tribes and by DOI	3,003.2	2,880.7

Tribal and Other Trust Funds
Statement of Changes in Trust Fund Balances – Cash Basis
for the Fiscal Years Ended September 30

(In millions of dollars)	2008	2007
Receipts	371.2	339.2
Interest received	133.1	139.3
Gain (loss) on disposition of investments, net	1.6	0.6
Disbursements	(383.3)	(519.6)
Increase (decrease) in trust fund balances, net	122.6	(40.5)
Trust fund balances, beginning of year	2,880.6	2,921.2
Trust fund balances, end of year	3,003.2	2,880.7

DOI has responsibility for the assets held in trust on behalf of American Indian tribes and individual Indian monies. DOI, through the Office of the Special Trustee (OST), holds trust funds in accounts for Indian tribes. It maintains over 2,700 accounts for Tribal and Other Trust Funds (including the Alaska Native Escrow Fund). The OST was established by the American Indian Trust Fund Management Reform Act of 1994 (Public Law 103-412) and was created to improve the accountability and management of Indian funds held in trust by the Government.

The balances that have accumulated in the Tribal and Other Trust Funds have resulted from judgment awards, settlements of claims, land use agreements, royalties on natural resource depletion, and other proceeds derived directly from trust resources and investment income.

The trust fund balances included in the Trust Funds Held for Indian Tribes and Other Trust Funds contain two categories: trust funds held for Indian tribes (considered non-Federal funds) and trust funds held by DOI for future transfer to a tribe upon satisfaction of certain conditions or where the Corpus of the fund is non-expendable (considered Federal funds).

The tables above depict the U.S. Government as trustee for Indian Trust Funds Held for Indian Tribes and Other Trust Funds. The Other Trust Funds included in the tables ($299.9 million and $289.9 million as of September 30, 2008, and 2007, respectively, identified in DOI's financial statements) and trust funds considered Federal funds are included in DOI's financial statements, and other DOI special reports.

OST also maintains about 378,000 open Individual Indian Monies (IIM) accounts. The IIM fund is primarily funds on deposit for individuals who have a beneficial interest in the trust funds. The IIM account-holders realize receipts primarily from royalties on natural resource depletion, land use agreements, and enterprises that have a direct relationship to trust fund resources and investment income. Funds related to the IIM Trust Fund are included in the following tables.

U.S. Government as Trustee for Indian Trust Funds Held for Individual Indian Monies Trust Funds – Modified Cash Basis Statement of Assets and Trust Fund Balances as of September 30

(In millions of dollars)	2008	2007
Assets:		
Cash and Cash Equivalents	49.3	48.3
Investments	391.8	372.6
Accrued interest receivable	3.1	2.8
Total Assets	444.2	423.7
Trust fund balances, held for individual Indians	444.2	423.7

Individual Indian Monies Trust Funds Statement of Changes in Trust Fund Balances – Modified Cash Basis for the Fiscal Years Ended September 30

(In millions of dollars)	2008	2007
Receipts	437.9	303.7
Interest received	21.6	20.8
Gain (loss) on disposition of investments, net	0.3	0.4
Disbursements	(439.3)	(319.5)
Increase (decrease) in trust fund balances, net	20.5	5.4
Trust fund balances, beginning of year	423.7	418.3
Trust fund balances, end of year	444.2	423.7

The amounts presented in the four tables of this note were prepared using a cash basis of accounting, which is a comprehensive basis of accounting other than GAAP. Receivables and payables are not recorded, and investment premiums and discounts are not amortized in the Trust Funds Held for Indian Tribes and Other Trust Funds. Receipts are recorded when received and disbursements when paid and investments are stated at historical cost. The only basis of accounting difference between the Trust Funds Held for Indian Tribes and Other Trust Funds and the IIM Trust Fund is that the latter records the receivables and payables related to accrued interest and dividends when earned, including amortization of investment discounts and premiums, and investments are stated at amortized cost.

Note 23. Social Insurance

Social Insurance Programs Trust Fund Balances

******UNAUDITED*******

(In billions of dollars)	2008	2007	2006	2005	2004
Social Security	2,238	2,048	1,859	1,687	1,531
Medicare:					
HI	312	300	285	268	256
SMI Part B	53	38	23	19	24
SMI Part D	3	1	-	-	-
Railroad Retirement	33	32	30	28	26
Black Lung	(10)	(10)	(10)	(9)	(8)

The Statement of Social Insurance presents the projected actuarial present value of the estimated future revenue and estimated future expenditures of the Social Security, Medicare, Railroad Retirement, and Black Lung social insurance programs which are administered by the SSA, HHS, RRB, and DOL, respectively. These estimates are based on the economic and demographic assumptions presented later in this note as set forth in the relevant Social Security and Medicare trustees' reports and in the agency financial report of HHS and in the relevant agency performance and accountability reports for SSA, RRB, and DOL (Black Lung). The projections are based on the continuation of program provisions contained in current law. The estimates in the consolidated Statements of Social Insurance are for persons who are participants or eventually will participate in the programs as contributors (workers) or beneficiaries (retired workers, survivors, and disabled) during the 75-year projection period (Black Lung is projected only through September 30, 2040, when the program will terminate).

Contributions and earmarked taxes consist of payroll taxes from employers, employees, and self-employed persons; revenue from Federal income taxation of Old-Age and Survivors Disability Insurance (OASDI) and railroad retirement benefits; excise tax on coal (Black Lung); and premiums from, and State transfers on behalf of, participants in Medicare. Income for all programs is presented from a consolidated perspective. Future interest payments and other future intragovernmental transfers have been excluded upon consolidation. Expenditures include scheduled benefit payments and administrative expenses. Scheduled benefits are projected based on the benefit formulas under current law. However, current Social Security and Medicare law does not provide for full benefit payments after the trust funds are exhausted.

Actuarial present values of estimated future revenue (excluding interest) and estimated future expenditures for the Social Security, Medicare, and Railroad Retirement social insurance programs are presented for three different groups of participants: (1) current participants who have attained eligibility age, (2) current participants who have not attained eligibility age, and (3) future participants who are new entrants expected to become participants in the future. Current participants in the Social Security and Medicare programs form the "closed group" of taxpayers and/or beneficiaries who are at least age 15 at the start of the projection period. For the 2007 Medicare projections, current participants are at least 18 years of age at the beginning of the projection period. Since the projection period for the Social Security, Medicare, and Railroad Retirement social insurance programs consists of 75 years, the period covers virtually all of the current participants' working and retirement years, a period that could be greater than 75 years in a relatively small number of instances. Future participants for Social Security and Medicare include births during the projection period and individuals below age 15 (below age 18 for the Medicare programs for 2007) as of January 1 of the valuation year. Railroad Retirement's future participants are the projected new entrants as of January 1 of the valuation year.

The present values of future expenditures in excess of future revenue are the current amounts of funds needed to cover projected shortfalls, excluding the starting trust fund balances, over the projection period. They are calculated by subtracting the actuarial present values of future scheduled contributions and dedicated tax income by and on behalf of current and future participants from the actuarial present value of the future scheduled benefit payments to them or on their behalf.

The trust fund balances as of the valuation date for the respective programs, including interest earned, are in the table shown above. Substantially all of the Social Security (OASDI) and Medicare Hospital Insurance (HI), and Supplementary Medical Insurance (SMI) trust fund balances consist of investments in special non-marketable U.S. Treasury securities that are guaranteed for principal and interest by the full faith and credit of the U.S. Government.

Social Security

The OASDI program, created in 1935, collectively referred to as "Social Security," provides cash benefits for eligible U.S. citizens and residents. Eligibility and benefit amounts are determined under the laws applicable for the period. Current law provides that the amount of the monthly benefit payments for workers, or their eligible dependents or survivors, is based on the workers' lifetime earnings histories.

The primary financing of the OASDI Trust Funds are taxes paid by workers, their employers, and individuals with self-employment income, based on work covered by the OASDI Program. Refer to the *Social Insurance* segment in the Supplemental Information section for additional information on social security program financing.

That portion of each trust fund not required to pay benefits and administrative costs is invested, on a daily basis, in interest-bearing obligations of the U.S. Government. The Social Security Act authorizes the issuance by the Treasury of special nonmarketable, intragovernmental debt obligations for purchase exclusively by the trust funds. Although the special issues cannot be bought or sold in the open market, they are redeemable at any time at face value and thus bear no risk of fluctuation in principal value due to changes in market yield rates. Interest on the bonds is credited to the trust funds and becomes an asset to the funds and a liability to the General Fund of the Treasury. These Treasury securities and related interest are eliminated in consolidation at the Governmentwide level.

Medicare

The Medicare Program, created in 1965, has two separate trust funds: the Hospital Insurance (HI, Medicare Part A) and Supplementary Medical Insurance (SMI, Medicare Parts B and D) Trust Funds. HI pays for inpatient acute hospital services and major alternatives to hospitals (skilled nursing services, for example) and SMI pays for hospital outpatient services, physician services, and assorted other services and products through the Part B account and pays for prescription drugs through the Part D account. Though the events that trigger benefit payments are similar, HI and SMI have different earmarked financing structures. Similar to OASDI, HI is financed primarily by payroll contributions. Other income to the HI fund includes a small amount of premium income from voluntary enrollees, a portion of the Federal income taxes that beneficiaries pay on Social Security benefits and interest credited on Treasury securities held in the HI Trust Fund. These Treasury securities and related interest are excluded in the consolidation at the Governmentwide level.

For SMI, transfers from the General Fund of the Treasury represent the largest source of income for both Parts B and D. Beneficiaries finance the remainder of Parts B and D costs via monthly premiums to these programs. With Part D drug coverage, Medicaid will no longer be the primary payer for beneficiaries dually eligible for Medicare and Medicaid. For those beneficiaries, States must pay the Part D account a portion of their estimated foregone drug costs for this population (referred to as State transfers). As with HI, interest received on Treasury securities held in the SMI Trust Fund is credited to the fund and these Treasury securities and related interest are eliminated in consolidation at the Governmentwide level. Refer to the *Social Insurance* segment in the Supplemental Information section for additional information on Medicare program financing.

The Medicare Modernization Act (MMA), enacted on December 8, 2003, created the Part D account in the SMI Trust Fund to account for the prescription drug benefit that began in 2006. The MMA established within SMI two Part D accounts related to prescription drug benefits: the Medicare Prescription Drug Account and the Transitional Assistance Account. The Medicare Prescription Drug Account was used in conjunction with the broad, voluntary prescription drug benefits that commenced in 2006. The Transitional Assistance Account was used to provide transitional assistance benefits, beginning in 2004 and extending through 2005, for certain low-income beneficiaries prior to the start of the new prescription drug benefit.

SMI Part B Physician Update Factor

The projected Part B expenditure growth reflected in the accompanying 2008 Statement of Social Insurance is significantly reduced as a result of the structure of physician payment updates under current law. In the absence of legislation, this structure would result in multiple years of significant reductions in physician payments, totaling an estimated 41 percent over the next 9 years. Reductions of this magnitude are not feasible and are very unlikely to occur fully in practice. For example, Congress has overridden scheduled negative updates for each of the last 6 years in practice. However, since these reductions are required in the future under the current-law payment system, they are reflected in the accompanying 2008 Statement of Social Insurance as required under GAAP. Consequently, the projected actuarial present values of Part B expenditure shown in the accompanying 2008 Statement of Social Insurance, is likely understated.

The potential magnitude of the understatement of Part B expenditures due to the physician payment mechanism can be illustrated using two hypothetical examples of changes to current law. These examples were developed by management for illustrative purposes only; the calculations have not been audited, and the examples do not attempt to portray likely or recommended future outcomes. Thus, the illustrations are useful only as general indicators of the substantial impacts that could result from future legislation on physician payments under Medicare and of the broad range of uncertainty associated with such impacts. Under current law, the projected 75-year present value of future Part B expenditures is $21.2 trillion. An alternative scenario indicated that if Congress were to set future physician payment updates at zero percent per year, then absent other provisions to offset these costs, the projected present value would increase to $23.4 trillion. Similarly, if Congress were to set future physician payment updates equal to the Medicare Economic Index (projected to be 2 to 2.5 percent per year), the present value would be $25.4 trillion.

The extent to which actual future Part B costs could exceed the projected current-law amounts due to physician payments depends on both the level of physician payment updates that might be legislated and on whether Congress would pass further provisions to help offset such costs (as it did, for example, in the Deficit Reduction Act in 2005 and the Medicare Improvements for Patients and Providers Act of 2008). As noted, these examples only reflect hypothetical changes to physician payments. It is likely that in the coming years, Congress will consider and pass numerous other legislative proposals affecting Medicare. Many of these would likely be designed to reduce costs in an effort to make the program more affordable. In practice, it is not possible to anticipate what actions Congress might take, either in the near term or over longer periods.

Medicare Improvements for Patients and Providers Act of 2008

On July 15, 2008, the Medicare Improvements for Patients and Providers Act (MIPPA) of 2008 was enacted. There were many provisions in MIPPA that affected the Medicare program. These include beneficiary improvements, such as expanded access to care, enrollment assistance and increased coverage. There were also provisions affecting payments to providers, such as physicians and managed care plans. The net overall impact of all MIPPA provisions over the 10-year period from fiscal years 2009-2018 is roughly $25 billion (unaudited) in increased Medicare spending. This represents less than 0.5 percent of total Medicare spending during the same time period.

The long-range financial projections underlying the Medicare projections in the 2008 Statement of Social Insurance are drawn from the Annual Report of the Medicare Board of Trustees to Congress, which was issued on March 25, 2008. These projections are based on an assumption that the Medicare laws, regulations, and policies in effect on that date will continue indefinitely without modification. In practice, the subsequent enactment of MIPPA will have an effect on Medicare expenditures and revenues. Due to the timing, complexity, and scope of the legislation, it is not possible to incorporate the impact of MIPPA into the long-range SOSI projections. The short-range estimates of the Medicare costs and savings under MIPPA, summarized above, provided an indication of the relative financial effect of the legislation. As stated above, the impact these provisions would have on the projections presented in the SOSI are relatively minor.

Social Security and Medicare – Demographic and Economic Assumptions

The Boards of Trustees[1] of the OASDI and Medicare Trust Funds provide in their annual reports to Congress short-range (10-year) and long-range (75-year) actuarial estimates of each trust fund. Because of the inherent uncertainty in estimates for 75 years into the future, the Boards use three alternative sets of economic and demographic assumptions to show a range of possibilities. Assumptions are made about many economic and demographic factors, including gross domestic product (GDP), earnings, the CPI, the unemployment rate, the fertility rate, immigration, mortality, disability incidence and terminations and, for the Medicare projections, health care cost growth. The assumptions used for the most recent set of projections shown in Tables 1A (Social Security) and Table 1B (Medicare) are generally referred to as the "intermediate assumptions," and reflect the trustees' best estimate of expected future experience. For further information on Social Security and Medicare demographic and economic assumptions, refer to SSA's performance and accountability report and HHS' agency financial report.

[1] There are six trustees: the Secretaries of the Treasury (managing trustee), Health and Human Services, and Labor; the Commissioner of the Social Security Administration; and two public trustees who are generally appointed by the President and confirmed by the Senate for a 4-year term. By law, the public trustees are members of two different political parties.

Table 1A
Social Security – Demographic and Economic Assumptions

Demographic Assumptions

Year	Total Fertility Rate [1]	Age-Sex Adjusted Death Rate [2] (per 100,000)	Net Immigration [3] (persons)	Period Life Expectancy at Birth [4] Male	Female
2008	2.06	822.2	1,250,000.0	75.4	79.9
2010	2.06	812.2	1,195,000.0	75.7	80.0
2020	2.03	750.5	1,130,000.0	76.9	80.9
2030	2.01	689.8	1,085,000.0	78.0	81.8
2040	2.00	635.9	1,050,000.0	79.0	82.6
2050	2.00	588.6	1,035,000.0	80.0	83.4
2060	2.00	546.8	1,030,000.0	80.8	84.2
2070	2.00	509.8	1,025,000.0	81.7	84.9
2080	2.00	476.8	1,025,000.0	82.4	85.6

Economic Assumptions

Year	Real Wage Differential [5] (percent)	Average Annual Wage in Covered Employment [6] (percent change)	CPI [7] (percent change)	Real GDP [8] (percent change)	Total Employment [9] (percent change)	Average Annual Interest Rate [10] (percent)
2008	1.3	4.1	2.8	2.3	0.4	4.4
2010	1.3	4.0	2.8	2.7	0.9	5.6
2020	1.1	3.9	2.8	2.2	0.5	5.7
2030	1.1	3.9	2.8	2.1	0.4	5.7
2040	1.1	3.9	2.8	2.2	0.5	5.7
2050	1.1	3.9	2.8	2.1	0.4	5.7
2060	1.1	3.9	2.8	2.1	0.4	5.7
2070	1.1	3.9	2.8	2.1	0.4	5.7
2080	1.1	3.9	2.8	2.1	0.4	5.7

[1] The total fertility rate for any year is the average number of children who would be born to a woman in her lifetime if she were to experience the birth rates by age observed in, or assumed for, the selected year, and if she were to survive the entire childbearing period. The ultimate total fertility rate of 2.0 is assumed to be reached in 2032.
[2] The age-sex-adjusted death rate is the crude rate that would occur in the enumerated total population as of April 1, 2000, if that population were to experience the death rates by age and sex assumed for the selected year. The death rate is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.
[3] Net immigration is the number of persons who enter during the year (both legally and otherwise) minus the number of persons who leave during the year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.
[4] The period life expectancy for a group of persons born in a given year is the average that would be attained by such persons if the group were to experience in succeeding years the death rates by age observed in, or assumed for, the given year. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.
[5] The real-wage differential is the difference between the percentage increases, before rounding, in the average annual wage in covered employment, and the average annual CPI.
[6] The average annual wage in covered employment is the total amount of wages and salaries for all employment covered by the OASDI program in a year divided by the number of employees with any such earnings during the year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.
[7] The CPI is the annual average value for the calendar year of the CPI for urban wage earners and clerical workers.
[8] The real GDP is the value of total output of goods and services, expressed in 2000 dollars. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.
[9] Total employment represents total of civilian and military employment in the U.S. economy. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.
[10] The average annual interest rate is the average of the nominal interest rates, which, in practice, are compounded semiannually for special-issue Treasury obligations sold only to the trust funds in each of the 12 months of the year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.

Table 1B
Medicare – Demographic and Economic Assumptions

Year	Demographic Assumptions: Total Fertility Rate[1]	Age-Sex Adjusted Death Rate[2] (per 100,000)	Net Immigration[3] (persons)
2008	2.06	822.2	1,250,000
2010	2.06	812.2	1,195,000
2020	2.03	750.5	1,130,000
2030	2.01	689.8	1,085,000
2040	2.00	635.9	1,050,000
2050	2.00	588.6	1,035,000
2060	2.00	546.8	1,030,000
2070	2.00	509.8	1,025,000
2080	2.00	476.8	1,025,000

Economic Assumptions

Year	Real Wage Differential[4] (percent)	Average Annual Wage in Covered Employment (percent change)	CPI[5] (percent change)	Real GDP[6] (percent)	Per Beneficiary Cost (percent change)[7]: HI	SMI: Part B	SMI: Part D	Real Interest Rate[8] (percent)
2008	1.3	4.1	2.8	2.3	7.1	1.4	2.9	1.9
2010	1.3	4.0	2.8	2.7	4.3	3.8	6.4	2.3
2020	1.1	3.9	2.8	2.2	4.3	6.1	7.8	2.9
2030	1.1	3.9	2.8	2.1	5.6	5.8	5.7	2.9
2040	1.1	3.9	2.8	2.2	5.9	5.5	5.3	2.9
2050	1.1	3.9	2.8	2.1	4.9	4.9	5.0	2.9
2060	1.1	3.9	2.8	2.1	4.8	4.8	4.7	2.9
2070	1.1	3.9	2.8	2.1	4.7	4.6	4.5	2.9
2080	1.1	3.9	2.8	2.1	4.4	4.3	4.4	2.9

[1] The total fertility rate for any year is the average number of children who would be born to a woman in her lifetime if she were to experience the birth rates by age observed in, or assumed for, the selected year, and if she were to survive the entire childbearing period. The ultimate total fertility rate of 2.0 is assumed to be reached in 2032.
[2] The age-sex-adjusted death rate is a weighted average of age-sex-specific death rates (deaths per 100,000) in a year where the weights are the number of people in the corresponding age-sex group as of April 1, 2000. The death rate is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.
[3] Net immigration is the number of persons who enter during the year (both legally and otherwise) minus the number of persons who leave during the year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.
[4] The real-wage differential is the difference between the percentage increases, before rounding, in the average annual wage in covered employment, and the average annual CPI.
[5] The CPI is the annual average value for the calendar year of the CPI for urban wage earners and clerical workers.
[6] The real GDP is the value of total output of goods and services, expressed in 2000 dollars. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.
[7] These increases reflect the overall impact of more detailed assumptions that are made for each of the different types of service provided by the Medicare program (for example, hospital care, physician services, and pharmaceutical costs). These assumptions include changes in the payment rates, utilization, and intensity of each type of service.
[8] The average annual interest rate earned on new trust fund securities, above and beyond the rate of inflation.

Railroad Retirement

The Railroad Retirement and Survivor Benefit program pays full retirement annuities at age 60 to railroad workers with 30 years of service. The program pays disability annuities based on total or occupational disability. It also pays annuities to spouses, divorced spouses, widow(er)s, remarried widow(er)s, surviving divorced spouses, children, and parents of deceased railroad workers. Medicare covers qualified railroad retirement beneficiaries in the same way as it does Social Security beneficiaries. The Railroad Retirement and Survivors' Improvement Act of 2001 (RRSIA) liberalized benefits for 30-year service employees and their spouses, eliminated a cap on monthly benefits for retirement and disability benefits, lowered minimum service requirements from 10 to 5 years, and provided for increased benefits for widow(er)s.

The RRB and the SSA share jurisdiction over the payment of retirement and survivor benefits. RRB has jurisdiction if the employee has at least 5 years (if performed after 1995) of railroad service. For survivor benefits, RRB requires that the employee's last regular employment before retirement or death be in the railroad industry. If a railroad employee or his or her survivors do not qualify for railroad retirement benefits, the RRB transfers the employee's railroad retirement credits to SSA.

Payroll taxes paid by railroad employers and their employees are a primary source of income for the Railroad Retirement and Survivor Benefit Program. By law, railroad retirement taxes are coordinated with Social Security taxes. Employees and employers pay tier I taxes at the same rate as Social Security taxes. Tier II taxes finance railroad retirement benefit payments that are higher than Social Security levels.

Other sources of program income include: financial transactions with the Social Security and Medicare Trust Funds, earnings on investments, Federal income taxes on railroad retirement benefits, and appropriations (provided after 1974 as part of a phase out of certain vested dual benefits). The financial interchanges and transactions between RRB's Social Security Equivalent Benefit (SSEB) Account, the Federal Old-Age and Survivors Insurance Trust Fund, the Disability Insurance Trust Fund, and the Federal Hospital Insurance Trust Fund are intended to put the latter three trust funds in the same position they would have been had railroad employment been covered under the Social Security Act. From a Governmentwide perspective, these future financial interchanges and transactions are intragovernmental transfers and are excluded in consolidation.

Railroad Retirement – Employment, Demographic and Economic Assumptions

The most recent set of projections are prepared using employment, demographic and economic assumptions and reflect the Board Members' best estimate of expected future experience.

Three employment assumptions were used in preparing the projections and reflect optimistic, moderate and pessimistic future passenger rail and freight employment. The average railroad employment is assumed to be 231,000 in 2008. This employment assumption, based on a model developed by the Association of American Railroads, assumes that (1) passenger service employment will remain at the level of 43,000 and (2) the employment base, excluding passenger service employment, will decline at a constant 2.5 percent annual rate for 25 years, at a falling rate over the next 25 years, and remain level thereafter. All the projections are based on an open group (i.e., future entrants) population.

The moderate (middle) economic assumptions include a long-term cost of living increase of 3.0 percent, an interest rate of 7.5 percent, and a wage increase of 4 percent. The cost of living assumption reflects the expected level of price inflation. The interest rate assumption reflects the expected return on NRRIT investments. The wage increase reflects the expected increase in railroad employee earnings.

Sources of the demographic assumptions including mortality rates and total termination rates, remarriage rates for widows, retirement rates and withdrawal rates, are listed in Table 2. For further details on the employment, demographic, economic and all other assumptions, refer to the *Railroad Retirement System Annual Report*, June 2008 and the 23rd *Actuarial Valuation of the Assets and Liabilities under the Railroad Retirement Acts* (Valuation Report) as of December 31, 2004, with Technical Supplement.

Table 2
Railroad Retirement Demographic Actuarial Assumptions (Sources)

Mortality Rates[1]	Mortality after age retirement	2004 RRB Annuitants Mortality Table
	Mortality after disability retirement	2004 RRB Disabled Mortality Table for Annuitants with Disability Freeze
		2004 RRB Disabled Mortality Table for Annuitants without Disability Freeze
	Mortality during active service	1994 RRB Active Service Mortality Table
	Mortality of widow annuitants	1995 RRB Mortality Table for Widows
Total Termination Rates[2]	Termination for spouses	2004 RRB Spouse Total Termination Table
	Termination for disabled children	2004 RRB Total Termination Table for Disabled Children
Widow Remarriage Rate[3]	1997 RRB Remarriage Table	
Retirement Rates[4]	Age retirement	See the Valuation Report
	Disability retirement	See the Valuation Report
Withdrawal Rates[5]	See the Valuation Report	

[1] These mortality tables are used to project the termination of eligible employee benefit payments within the population.
[2] Total termination rates are used to project the termination of dependent benefits to spouses and disabled children.
[3] This rate is used to project the termination of spousal survivor benefits.
[4] The retirement rates are used to determine the expected annuity to be paid based on age and years of service for both age and disability retirees.
[5] The withdrawal rates are used to project all withdrawals from the railroad industry and resultant effect on the population and accumulated benefits to be paid.

Black Lung Disability Benefit Program

The Black Lung Disability Benefit Program provides medical and survivor benefits for eligible coal miners who are disabled due to pneumoconiosis (black lung disease) as a result of their coal mine employment. The DOL operates the Black Lung Disability Benefit Program. The Black Lung Disability Trust Fund (BLDTF) provides benefit payments to eligible coal miners disabled by pneumoconiosis when no responsible mine operator can be assigned the liability.

Excise taxes on coal mine operators, based on the sale of coal, are the primary source of financing black lung disability payments and related administrative costs. Though excise tax revenues currently exceed costs (and are expected to in the future), that was not always the case. The Black Lung Benefits Revenue Act provides for repayable advances to the BLDTF from the General Fund of the Treasury, in the event that BLDTF resources are not adequate to meet program obligations. During earlier years of the program, general revenues were needed to pay for cash shortfalls in the program.

Black Lung – Demographic and Economic Assumptions

The demographic assumptions used for the most recent set of projections are the number of beneficiaries and their life expectancy. The beneficiary population data is updated from information supplied by the program. The beneficiary population is a nearly closed universe in which attrition by death exceeds new entrants by a ratio of more than ten to one. Life tables are used to project the life expectancies of the beneficiary population.

The economic assumptions used for the most recent set of projections are coal excise tax revenue estimates, the tax rate structure, Federal civilian pay raises, medical cost inflation, and the interest rate on new repayable advances from the Treasury.

Estimates of future receipts of the black lung excise tax are based on projections of future coal production and sale prices prepared by the Energy Information Agency of DOE. Treasury's Office of Tax Analysis provides the first 11 years of tax receipt estimates. The remaining years are estimated using a growth rate based on both historical tax receipts and Treasury's estimated tax receipts. The coal excise tax rate structure is $1.10 per ton of underground-mined coal and $0.55 per ton of surface-mined coal sold, with a cap of 4.4 percent of sales price, through December 31, 2013. Starting in 2014, the tax rates revert to $0.50 per ton of underground-mined coal and $0.25 per ton of surface-mine coal sold, and a limit of 2 percent of sales price.

OMB supplies assumptions for future monthly benefit rate increases based on increases in the Federal pay scale and future medical cost inflation based on increases in the consumer price index-medical, which are used to calculate future benefit costs. During the current projection period, future benefit rate increases 2.4 percent in each year, and medical cost increases 3.9 percent each year. Estimates for administrative costs for the first 11 years of the projection are supplied by DOL's Budget Office, while later years are based on the number of projected beneficiaries. Estimates for future interest on advances are based on the interest rates on outstanding advances ranging from 4.3 percent to 13.9 percent and new borrowings ranging from 4.9 percent to 5.6 percent.

Note 24. Stewardship Land and Heritage Assets

Stewardship land is Federally-owned land that is set aside for the use and enjoyment of present and future generations, and land on which military bases are located. Except for military bases, this land is not used or held for use in general Government operations. Stewardship land is land that the Government does not expect to use to meet its obligations, unlike the assets listed in the Balance Sheets. Stewardship land is measured in non-financial units such as acres of land and lakes, number of National Parks and square miles of National Marine Sanctuaries. Examples of stewardship land include national parks, national forests, wilderness areas, and land used to enhance ecosystems to encourage animal and plant species, and to conserve nature. This category excludes lands administered by the Bureau of Indian Affairs and held in trust.

Most stewardship land managed by the Government was once part of the 1.8 billion acres of public domain land acquired between 1781 and 1867. Stewardship land accounts for 28 percent of the current U.S. landmass.

DOI uses units as a measure to more accurately reflect the major categories of uses of stewardship land. As of September 30, 2008, they have 548 national wildlife refuges, 378 park units, 134 geographic management areas, 67 fish hatcheries, and many other categories. At the end of fiscal year 2008, the Department of Agriculture's Forest Service managed an estimated 193 million acres of public land, while the Department of Commerce (DOC) had 13 National Marine Sanctuaries, which included near–shore coral reefs and open ocean, covering a total of 19 thousand square miles.

Stewardship lands are used and managed in accordance with the statutes authorizing their acquisition or directing their use and management. Additional detailed information concerning stewardship land can be obtained in the financial statements of DOI, DOC, DOD, and USDA.

Heritage assets are Government-owned assets that have one or more of the following characteristics:

- Historical or natural significance.
- Cultural, educational, or artistic importance.
- Significant architectural characteristics.

The cost of heritage assets often is not determinable or relevant to their significance. Like stewardship land, the Government does not expect to use these assets to meet its obligations. The most relevant information about heritage assets is non-financial. The public entrusts the Government with these assets and holds it accountable for their preservation. Examples of heritage assets include the Mount Rushmore National Memorial and Yosemite National Park. Other examples of heritage assets include the Declaration of Independence, the U.S. Constitution, and the Bill of Rights preserved by the National Archives. Also included are national monuments/structures such as the Vietnam Veterans Memorial, the Jefferson Memorial, and the Washington Monument, as well as the Library of Congress. Many other sites such as battlefields, historic structures, and national historic landmarks are placed in this category, as well.

Many laws and regulations govern the preservation and management of heritage assets. Established policies by individual Federal agencies for heritage assets ensure the proper care and handling of the assets under their control and preserve these assets for the benefit of the American public.

Some heritage assets are used both to remind us of our heritage and for day-to-day operations. These assets are referred to as multi-use heritage assets. One typical example is the White House. The cost of acquisition, betterment or reconstruction of all multi-use heritage assets is capitalized as general property, plant, and equipment and is depreciated.

The Government classifies heritage assets into two broad categories: collection type and non-collection type. Collection type heritage assets include objects gathered and maintained for museum and library collections. Non-collection type heritage assets include national wilderness areas, wild and scenic rivers, natural landmarks, forests, grasslands, historic places and structures, memorials and monuments, buildings, national cemeteries and archeological sites.

The discussion of the Government's heritage assets is not all-inclusive. Rather, it highlights significant heritage assets reported by Federal agencies. Please refer to the individual financial statements of the DOI, the USDA, the National Archives and Records Administration, and the websites for the Library of Congress (http://www.loc.gov/index.html) and Smithsonian Institution (http://www.si.edu), for additional information on multi-use heritage assets, agency stewardship policies, and physical units by major categories and conditions.

Note 25. Subsequent Events

A. Emergency Economic Stabilization Act of 2008

The Emergency Economic Stabilization Act of 2008 (EESA) was signed into law on October 3, 2008. This law authorizes a Troubled Asset Relief Program (TARP) to be administered by the Department of the Treasury. The TARP is intended to promote market stability and protect the U.S. economy by authorizing Treasury to purchase and guarantee troubled mortgage-related assets and other financial assets. EESA also provides for the purchase of any other financial instruments that the Secretary of the Treasury determines, after consultation with the Federal Reserve Board Chairman, is necessary to purchase in order to promote financial market stability.

The Secretary of the Treasury's authority to purchase troubled assets was limited initially to $250 billion in outstanding assets, and increased to $350 billion upon certification by the President to the Congress on October 14, 2008. The authority can be increased to the maximum of $700 billion upon submission of a written report from the President to the Congress detailing the Secretary of the Treasury's plan to exercise additional authority, providing Congress does not enact a joint resolution disapproving the plan of the Secretary.

Upon establishment of the insurance program required under EESA the $700 billion limit shall be reduced by the difference between outstanding guaranteed obligations under the insurance program authorized by EESA, if any, and the balance in the Troubled Assets Insurance Financing Fund (TAIFF) established by EESA to guarantee timely payments on mortgage-related assets. The Treasury Secretary can guarantee timely payment of up to 100 percent of the principal and interest on these insured assets. Institutions seeking this guarantee will be required to pay risk-based premiums into the fund. The premiums will be in amounts determined by the Treasury Secretary, as necessary, to meet anticipated claims and eliminate any budgetary cost.

Significant EESA authorities terminate on December 31, 2009. However, the Treasury Secretary can extend this authority to October 3, 2010, upon submission of a written certification to Congress. EESA increases the statutory public debt limit by $700 billion, from $10.615 trillion to $11.315 trillion.

Upon passage of EESA, Treasury established the Office of Financial Stability to administer the TARP. No EESA transactions occurred during fiscal year 2008. As of December 9, 2008, over $200 billion in troubled assets were purchased or committed through TARP.

The EESA also provides for a temporary increase in the Federal Deposit Insurance Corporation (FDIC) deposit coverage from $100,000 per depositor to $250,000 per depositor from the date of the enactment of the legislation through December 31, 2009. This will significantly increase future contingent liabilities for anticipated failure of insured institutions. See FDIC's Annual Report, released on a calendar year basis, for more information.

EESA contains numerous tax provisions that could result in additional burdens to future deficits. EESA also amended the HOPE for Homeowners Program, established by HERA, which the Federal Housing Administration may guarantee up to $300 billion in mortgages.

The Federal Reserve announced a program to purchase up to $500 billion of mortgage-backed securities and up to $100 billion of Fannie and Freddie debt, and to lend up to $200 billion against new car, student, and small-business loans. Treasury has pledged $20 billion from TARP to cover partial loss.

The Reserve Fund's U.S. Government Money Market Fund (the "Fund"), which Treasury accepted into its temporary guarantee program for money market funds (see Note 8), has not made a claim to Treasury under the program. In a separate agreement with the Fund, the Treasury Exchange Stabilization Fund (ESF) has agreed to serve as a buyer of last resort for the Fund's portfolio, which consists of short-term U.S. Government and GSE securities. EESA contains a provision for reimbursement of the ESF for its funds used under the Temporary Guarantee Program for Money Market Funds, which would cover any losses, however unlikely, arising from the separate agreement with the Fund.

Under EESA, in November 2008, Treasury has committed to providing Citigroup another $20 billion from TARP. In addition, Treasury and FDIC agreed to share losses with Citigroup on a $306 billion asset pool for any losses in excess of $37 billion. Treasury and FDIC's combined maximum exposure is $15 billion, which may be offset by any value of the $7 billion of preferred stock issued to them by Citigroup. FRB will backstop residual risk in the asset pool through a nonrecourse loan.

Treasury's actions to stabilize the financial system and the economy continue as of the date of this Report. Treasury's strategy for continued implementation of the financial rescue package can be found at: http://www.treas.gov/initiatives/eesa/.

B. American International Group (AIG)

To help AIG work out its financial difficulties, the Federal Reserve agreed to lend up to $85 billion to AIG pursuant to the authority in Section 13(3) of the Federal Reserve Act. The Government is not a party to the AIG credit facility with the Federal Reserve, and has no liabilities, commitments, or guarantees pursuant to the Fed's arrangements with AIG or any other financial relationship with AIG.

Under the terms of the agreement with AIG and the Federal Reserve, an approximately 79.9 percent equity interest in AIG (in the form of Convertible Participating Serial Preferred Stock convertible into approximately 79.9 percent of the issued and outstanding shares of common stock) was to be issued to a trust to be established by the Federal Reserve. As of the date of this report, it is anticipated that the Treasury will be named as the beneficiary of that trust, so that when the stock is ultimately liquidated the proceeds will be deposited into the General Fund of the Government. Treasury would also be the recipient of any dividends and any proceeds from the liquidation of the stock on behalf of the General Fund. The accounting and reporting for any activities related to the government's interest in the stock held by the trust will be done by Treasury.

Subsequent to September 30, 2008, the credit facility to assist AIG was restructured significantly. Treasury agreed in November 2008 to directly purchase $40 billion in senior AIG preferred stock through the TARP, with the proceeds being used to pay down the Federal Reserve's $85 billion credit facility. Treasury will also receive common stock warrants for 2 percent of the outstanding AIG common stock, with the above-described convertible preferred stock interest to be owned by the trust reduced to 77.9 percent.

C. Energy Improvement and Extension Act of 2008

The Energy Improvement and Extension Act of 2008, enacted on October 3, 2008, allowed for a temporary increase in coal excise tax rates to continue an additional 5 years beyond the current statutory limit collected for the Black Lung Disability Trust Fund. The excise rates were set to decrease from $1.10 per ton for coal from underground mines and $0.55 per ton for coal from surface mines (not to exceed 4.4 percent of sales) to $0.50 per ton for coal from underground mines and $0.25 per ton for coal from surface mines (not to exceed 2 percent of sales) on January 1, 2014. The Act extended the temporary increase to December 31, 2018. The higher excise tax rates will continue until the earlier of December 31, 2018, or the first December 31 after 2007 in which there exist no (1) balances of repayable advances described in section 9501 of the Internal Revenue Code and (2) unpaid interest on the advances.

Section 113 of the Energy Improvement and Extension Act of 2008 also allowed a restructuring of the debt of the Black Lung Disability Trust Fund that resulted in an actuarial present value of future excise tax income during the projection period of $9,293 billion as of October 7, 2008, and an actuarial present value of the par value of the zero coupon bonds coming due during the projection period of $6,326 billion as of October 7, 2008. This, with an actuarial present value of $2,967 billion for expenses, results in a fund balance of zero at the end of the projection period.

D. Temporary Liquidity Guarantee Program

On October 14, 2008 the FDIC established the Temporary Liquidity Guarantee Program as part of a larger government effort to strengthen confidence and encourage liquidity in the banking system. The new program will (1) guarantee newly issued senior unsecured debt of eligible FDIC-insured depository institutions and certain holding companies between October 14, 2008 and June 30, 2009 with guarantees expiring no later than June 30, 2012, and (2) provide full deposit insurance coverage for non-interest bearing deposit transaction accounts in FDIC-insured institutions until December 31, 2009. The FDIC will charge a fee, based on a sliding scale from 50 to 100 basis points, depending on length of maturity, to guarantee newly-issued senior unsecured debt and a 10-basis point surcharge will be collected through the normal assessment cycle to cover the non-interest bearing transaction accounts.

E. Other

The ability of issuers of the debt securities held by the Government to meet their obligations may be affected by economic developments in a specific industry or region. The values of the securities can be significantly affected by changes in interest rates or in the financial condition of the issuer or market conditions generally. The Government invests a portion of its assets in mortgage-backed securities and debentures. The value and related income of these securities is sensitive to change in economic conditions, including delinquencies and/or defaults. Recent instability in the markets for fixed-income securities, particularly mortgage-backed securities, has resulted in increased volatility of market prices and periods of illiquidity have adversely impacted the valuation of certain securities held by the Government. The values of such investments are reported at their fair value based upon the market conditions as of September 30, 2008. Due to continued market instability since yearend, the fair values of such investments have decreased from the amounts reported.

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United States Government Supplemental Information (Unaudited) for the Years Ended September 30, 2008, and September 30, 2007

Social Insurance

The social insurance programs consisting of Social Security, Medicare, Railroad Retirement and Black Lung, were developed to provide income security and health care coverage to citizens under specific circumstances as a responsibility of the Government. Because taxpayers rely on these programs in their long-term planning, social insurance program information should indicate whether they are sustainable under current law, as well as what their effect will be on the Government's financial condition. The resources needed to run these programs are raised through taxes and fees. Eligibility for benefits rests in part on earnings and time worked by the individuals. Social Security benefits are generally redistributed intentionally toward lower-wage workers (i.e., benefits are progressive). In addition, each social insurance program has a uniform set of entitling events and schedules that apply to all participants.

Social Security and Medicare

Social Security

The Federal Old-Age and Survivors Insurance (OASI) Trust Fund was established on January 1, 1940, as a separate account in the Treasury. The Federal Disability Insurance (DI) Trust Fund, another separate account in the Treasury, was established on August 1, 1956. OASI pays cash retirement benefits to eligible retirees and their eligible dependents and survivors, and the much smaller DI fund pays cash benefits to eligible individuals who are unable to work due to medical conditions. Though the events that trigger benefit payments are quite different, both trust funds have the same earmarked financing structure: primarily payroll taxes and income taxes on benefits. All financial operations of the OASI and DI Programs are handled through these respective funds. The two funds are often referred to as simply the combined Old-Age and Survivors Disability Insurance (OASDI) Trust Funds. At the end of calendar year 2007, OASDI benefits were paid to approximately 49 million beneficiaries.

The primary financing of these two funds are taxes paid by workers, their employers, and individuals with self-employment income, based on work covered by the OASDI Program. Since 1990, employers and employees have each paid 6.2 percent of taxable earnings. The self-employed pay 12.4 percent of taxable earnings. Payroll taxes are computed on wages and net earnings from self-employment up to a specified maximum annual amount, referred to as maximum taxable earnings ($102,000 in 2008), that increases each year with economy-wide wages.

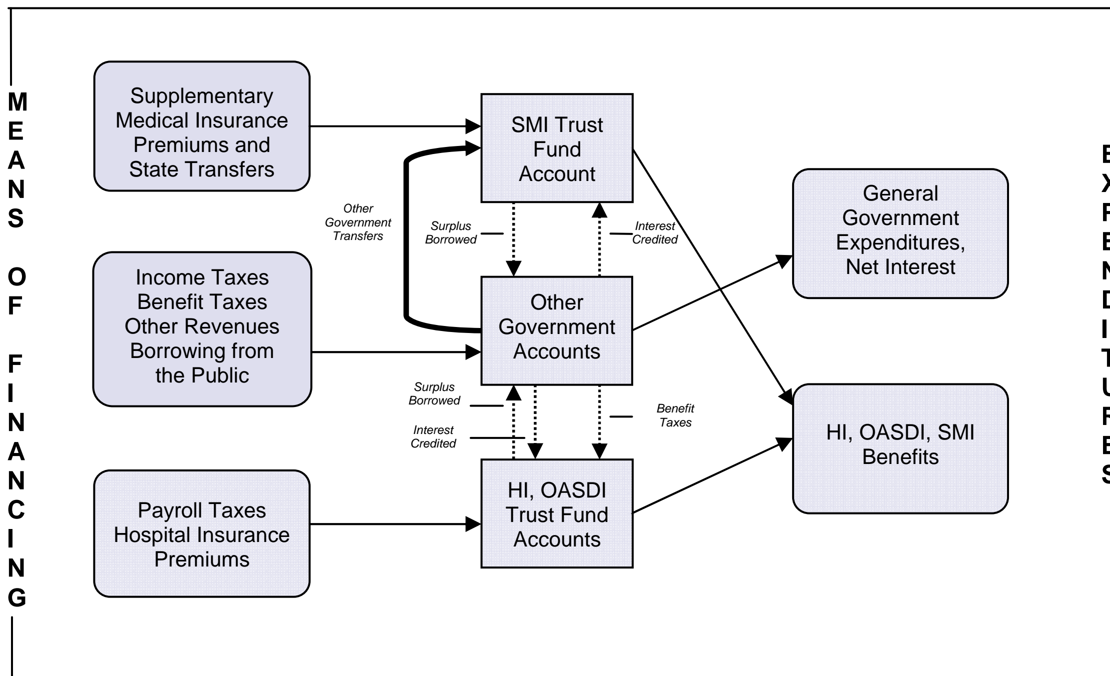
Since 1984, up to one-half of OASDI benefits have been subject to Federal income taxation. Effective for taxable years beginning after 1993, the maximum percentage of benefits subject to taxation was increased from 50 percent to 85 percent. The revenue from income taxes on up to 50 percent of benefits is allocated to the OASDI Trust Funds and the rest is allocated to the Hospital Insurance (HI) Trust Fund.

Medicare

The Medicare Program, created in 1965, also has two separate trust funds: the Hospital Insurance (HI, Medicare Part A) and Supplementary Medical Insurance (SMI, Medicare Parts B and D) Trust Funds.[1] HI pays for inpatient acute hospital services and major alternatives to hospitals (skilled nursing services, for example) and SMI pays for hospital outpatient services, physician services, and assorted other services and products through the Part B account and pays for prescription drugs through the Part D account. Though the events that trigger benefit payments are similar, HI and SMI have different earmarked financing structures. Similar to OASDI, HI is financed primarily by payroll contributions. Employers and employees each pay 1.45 percent of earnings, while self-employed workers pay 2.9 percent of their net earnings. Other income to the HI fund includes a small amount of premium income from voluntary enrollees, a portion of the Federal income taxes that beneficiaries pay on Social Security benefits (as explained above), and interest credited on Treasury securities held in the HI Trust Fund. These Treasury securities and related interest are excluded upon consolidation at the Governmentwide level.

For SMI, transfers from the General Fund of the Treasury represent the largest source of income covering about 74 percent and 79 percent of program costs for Parts B and D, respectively. Beneficiaries pay monthly premiums that finance approximately 26 percent and 21 percent of costs for Parts B and D, respectively. With Part D drug coverage, Medicaid will no longer be the primary payer for beneficiaries dually eligible for Medicare and Medicaid. For those beneficiaries, States must pay the Part D account a portion of their estimated foregone drug costs for this population (referred to as State transfers). As with HI, interest received on Treasury securities held in the SMI Trust Fund is credited to the fund. These Treasury securities and related interest are excluded upon consolidation at the Governmentwide level. Refer to Note 23—Social Insurance, for additional information on Medicare program financing.

Figure 1
Social Security, Medicare, and Governmentwide Finances



[1] Medicare legislation in 2003 created the new Part D account in the SMI Trust Fund to track the finances of a new prescription drug benefit that began in 2006. As in the case of Medicare Part B, approximately three-quarters of revenues to the Part D account will come from future transfers from the General Fund of the Treasury. Consequently, the nature of the relationship between the SMI Trust Fund and the Federal budget described below is largely unaffected by the presence of the Part D account though the magnitude will be greater.

Social Security, Medicare, and Governmentwide Finances

The current and future financial status of the separate Social Security and Medicare Trust Funds is the focus of the trustees' reports, a focus that may appropriately be referred to as the "trust fund perspective." In contrast, the Government primarily uses the *unified budget* concept as the framework for budgetary analysis and presentation. It represents a comprehensive display of all Federal activities, regardless of fund type or on- and off-budget status, and has a broader focus than the trust fund perspective that may appropriately be referred to as the "budget perspective" or the "Governmentwide perspective." Social Security and Medicare are among the largest expenditure categories of the U.S. Federal budget. Together, they now account for more than a third of all Federal spending and the percentage is projected to rise dramatically for the reasons discussed below. This section describes in detail the important relationship between the trust fund perspective and the Governmentwide perspective.

Figure 1 is a simplified graphical depiction of the interaction of the Social Security and Medicare Trust Funds with the rest of the Federal budget.[2] The boxes on the left show sources of funding, those in the middle represent the trust funds and other Government accounts (of which the General Fund is a part) into which that funding flows, and the boxes on the right show simplified expenditure categories. The figure is intended to illustrate how the various sources of program revenue flow through the budget to beneficiaries. The general approach is to group revenues and expenditures that are linked specifically to Social Security and/or Medicare separately from those for other government programs.

Each of the trust funds has its own sources and types of revenue. With the exception of General Fund transfers to SMI, each of these revenue sources is earmarked specifically for the respective trust fund, and cannot be used for other purposes. In contrast, personal and corporate income taxes and other revenue go into the General Fund of the Treasury and are drawn down for any Government program for which Congress has approved spending.[3] The arrows from the boxes on the left represent the flow of the revenues into the trust funds and other Government accounts.

The heavy line between the top two boxes in the middle of Figure 1 represents intragovernmental transfers between the SMI Trust Fund and other Government accounts. The Medicare SMI Trust Fund is shown separately from the two Social Security trust funds (OASI and DI) and the Medicare HI Trust Fund to highlight the unique financing of SMI. SMI is currently the only one of the four programs that is funded through transfers from the General Fund of the Treasury, which is part of the other Government accounts (the Part D account will receive transfers from the States). The transfers finance roughly three-fourths of SMI Program expenses. The transfers are automatic; their size depends on how much the program requires, not on how much revenue comes into the Treasury. If General Fund revenues become insufficient to cover both the mandated transfer to SMI and expenditures on other general Government programs, Treasury would have to borrow to make up the difference. In the longer run, if transfers to SMI are increasing—as shown below, they are projected to increase significantly in coming years—then Congress must either raise taxes, cut other Government spending, reduce SMI benefits, or borrow even more.

The dotted lines between the middle boxes of Figure 1 also represent intragovernmental transfers but those transfers arise in the form of "borrowing/lending" between the Government accounts. Interest credited to the trust funds arises when the excess of program income over expenses is loaned to the General Fund. The vertical lines labeled *Surplus Borrowed* represent these flows from the trust funds to the other Government accounts. These loans reduce the amount the General Fund has to borrow from the public to finance a deficit (or likewise increase the amount of debt paid off if there is a surplus). However, the General Fund has to credit interest on the loans from the trust fund programs, just as if it borrowed the money from the public. The credits lead to future obligations for the General Fund (which is part of the other Government accounts). These transactions are indicated in Figure 1 by the vertical arrows labeled *Interest Credited*. The credits increase trust fund income exactly as much as they increase credits (future obligations) in the General Fund. From the standpoint of the Government as a whole, at least in an accounting sense, these interest credits are a wash.

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[2] The Federal unified budget encompasses all Government financing and is synonymous with a Governmentwide perspective.

[3] Other programs also have dedicated revenues in the form of taxes and fees (and other forms of receipt) and there are a large number of earmarked trust funds in the Federal budget. Total trust fund receipts account for about 40 percent of total Government receipts with the Social Security and Medicare Trust Funds accounting for about two-thirds of trust fund receipts. For further discussion, see the report issued by the Government Accountability Office, *Federal Trust and Other Earmarked Funds*, GAO-01-199SP, January 2001. In the figure and the discussion that follows, all other programs, including these other earmarked trust fund programs, are grouped under "Other Government Accounts" to simplify the description and maintain the focus on Social Security and Medicare.

It is important to understand the additional implications of these loans from the trust funds to the other Government accounts. When the trust funds get the receipts that they loan to the General Fund, these receipts provide additional authority to spend on benefits and other program expenses. The General Fund, in turn, has taken on the obligation of paying interest on these loans every year and repaying the principal when trust fund income from other sources falls below expenditures—the loans will be called in and the General Fund will have to reduce other spending, raise taxes, or borrow more from the public to finance the benefits paid by the trust funds.

Actual dollar amounts roughly corresponding to the flows presented in Figure 1 are shown in Table 1 for fiscal year 2008. In Table 1, revenues from the public (left side of Figure 1) and expenditures to the public (right side of Figure 1) are shown separately from transfers between Government accounts (middle of Figure 1). Note that the transfers ($181.1 billion) and interest credits ($132.8 billion) received by the trust funds appear as negative entries under "Other Government" and are thus offsetting when summed for the total budget column. These two intragovernmental transfers are the key to the differences between the trust fund and budget perspectives.

From the Governmentwide perspective, only revenues received from the public (and States in the case of Medicare, Part D) and expenditures made to the public are important for the final balance. Trust fund revenue from the public consists of payroll taxes, benefit taxes, and premiums. For HI, the difference between total expenditures made to the public ($230.2 billion) and revenues ($213.2 billion) was ($17.1 billion) in 2008, indicating that HI had a relatively small negative effect on the overall budget outcome *in that year*. For the SMI account, revenues from the public (premiums) were relatively small, representing about a quarter of total expenditures made to the public in 2008. The difference ($163.6 billion) resulted in a net draw on the overall budget balance in that year. For OASDI, the difference between total expenditures made to the public ($617.0 billion) and revenues from the public ($689.0 billion) was $71.9 billion in 2008, indicating that OASDI had a positive effect on the overall budget outcome *in that year*.

The trust fund perspective is captured in the bottom section of each of the three trust fund columns. For HI, total expenditures exceeded total revenues by $0.5 billion in 2008, as shown at the bottom of the first column. This surplus would be added to the beginning trust fund (not shown) that leads to budget obligations in future years. For SMI, total revenues of $244.5 billion ($60.9 + $183.6), including $180.4 billion transferred from other Government accounts (the General Fund), exceeded total expenditures by $20 billion. Transfers to the SMI Program from other Government accounts (the General Fund), amounting to about 75 percent of program costs, are obligated under current law and therefore appropriately viewed as revenue from the trust fund perspective. For OASDI, total revenues of $802.7 billion ($689.0 + $113.7), including interest and a small amount of other Government transfers, exceeded total expenditures of $617.0 billion by $185.7 billion.

Table 1
Revenues and Expenditures for Medicare and Social Security Trust Funds and the Total Federal Budget, for the Fiscal Year ended September 30, 2008

	Trust Funds					
(In billions of dollars)	HI	SMI	OASDI	Total	All Other	Total [1]
Revenues from the public:						
Payroll and benefit taxes	208.9	-	689.0	897.9	-	897.9
Premiums	4.2	53.8	-	58.0	-	58.0
Other taxes and fees	-	7.0	-	7.0	1,561.0	1,568.0
Total	213.2	60.9	689.0	962.9	1,561.0	2,523.9
Total expenditures to the public [2]	230.2	224.5	617.0	1,071.7	1,907.0	2,978.7
Net results for budget perspective [3]	(17.1)	(163.6)	71.9	(108.8)	(346.0)	(454.8)
Revenues from other Government accounts:						
Transfers	0.7	180.4	-	181.1	(181.1)	-
Interest credits	15.9	3.2	113.7	132.8	(132.8)	-
Total	16.6	183.6	113.7	313.9	(313.9)	-
Net results for trust fund perspective [3]	(0.5)	20.0	185.7	205.2	N/A	N/A

[1] This column is the sum of the preceding two columns and shows data for the total Federal budget. The figure $454.8 billion was the total Federal deficit in fiscal year 2008.
[2] The OASDI figure includes $4.0 billion transferred to the Railroad Retirement Board for benefit payments and is therefore an expenditure to the public.
[3] Net results are computed as revenues less expenditures.

Notes: Amounts may not add due to rounding.
"N/A" indicates not applicable.

Cashflow Projections

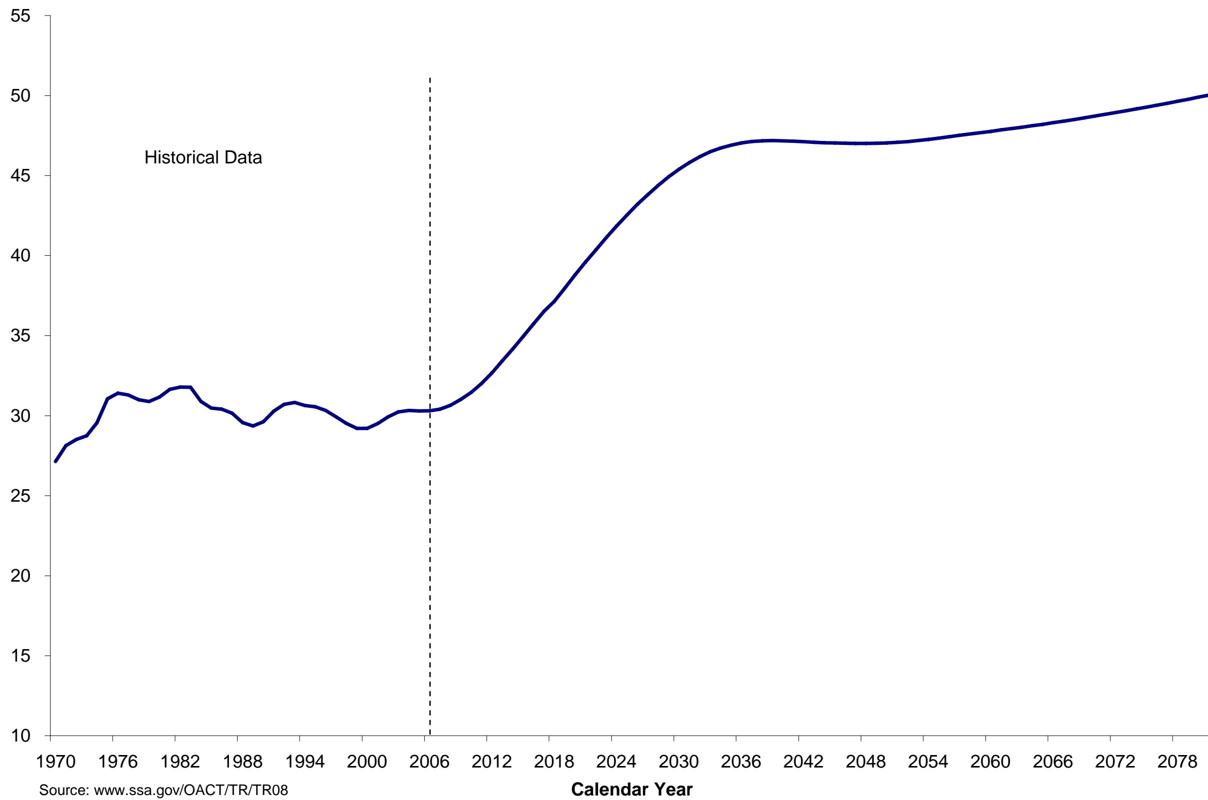
Background

Economic and Demographic Assumptions. The Boards of Trustees[4] of the OASDI and Medicare Trust Funds provide in their annual reports to Congress short-range (10-year) and long-range (75-year) actuarial estimates of each trust fund. Because of the inherent uncertainty in estimates for 75 years into the future, the Boards use three alternative sets of economic and demographic assumptions to show a range of possibilities. The economic and demographic assumptions used for the most recent set of intermediate projections for Social Security and Medicare are shown in the "Social Security" and "Medicare" sections of Note 23—Social Insurance.

[4] There are six trustees: the Secretaries of the Treasury (managing trustee), Health and Human Services, and Labor; the Commissioner of the Social Security Administration; and two public trustees who are appointed by the President and confirmed by the Senate for a 4-year term. By law, the public trustees are members of two different political parties.

Beneficiary-to-Worker Ratio. Underlying the pattern of expenditure projections for both the OASDI and Medicare Programs is the impending demographic change that will occur as the large baby-boom generation, born in the years 1946 to 1964, retires or reaches eligibility age. The consequence is that the number of beneficiaries will increase much faster than the number of workers who pay taxes that are used to pay benefits. The pattern is illustrated in Chart 1 which shows the ratio of OASDI beneficiaries to 100 covered workers for the historical period and estimated for the next 75 years. In 2007, there were about 30 beneficiaries for every 100 workers. By 2030, there will be about 45 beneficiaries for every 100 workers. A similar demographic pattern confronts the Medicare Program. For example, for the HI Program, there were about 26 beneficiaries for every 100 workers in 2008; by 2030, there are expected to be about 41 beneficiaries for every 100 workers. This ratio for both programs will continue to increase to about 50 beneficiaries for every 100 workers by the end of the projection period, after the baby-boom generation has moved through the Social Security system as well as declining birth rates and increasing longevity.

Chart 1—OASDI Beneficiaries per 100 Covered Workers 1970-2082

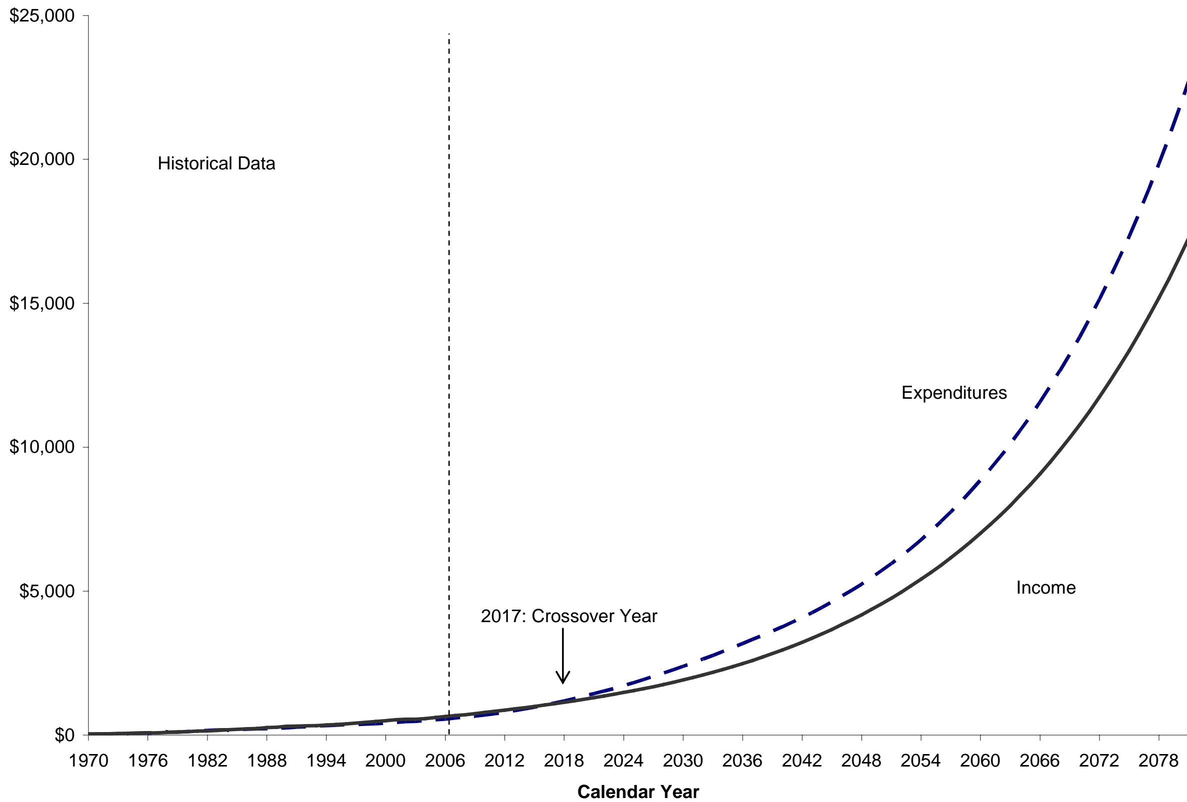


Social Security Projections

Nominal Income and Expenditures. Chart 2 shows historical values and actuarial estimates of combined OASDI annual income (excluding interest) and expenditures for 1970-2082 in nominal dollars. The estimates are for the open-group population. That is, the estimates include taxes paid from, and on behalf of, workers who will enter covered employment during the period, as well as those already in covered employment at the beginning of that period. These estimates also include scheduled benefit payments made to, and on behalf of, such workers during that period. Note that expenditure projections in Chart 2 and subsequent charts are based on current-law benefit formulas, regardless of whether the income and assets are available to finance them.

Chart 2—OASDI Income (Excluding Interest) and Expenditures 1970-2082

(In billions of nominal dollars)



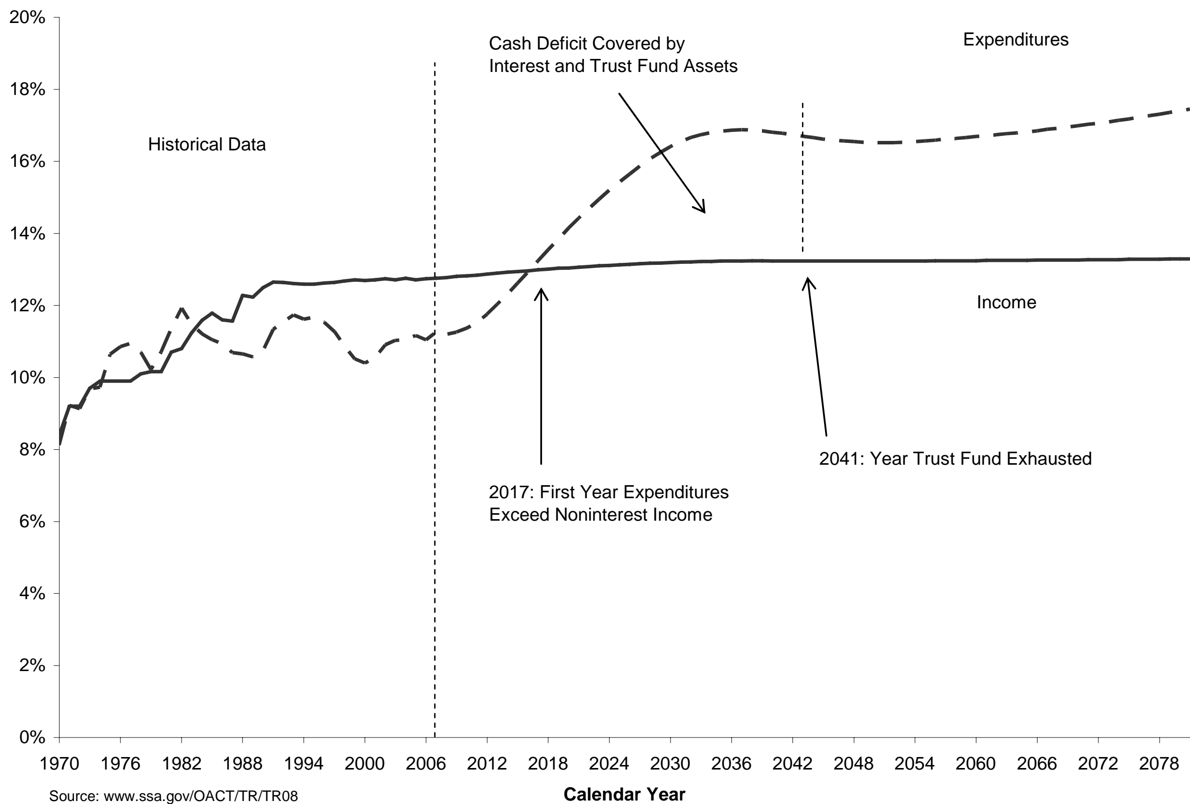
Source: www.ssa.gov/OACT/TR/TR08

Currently, Social Security tax revenues exceed benefit payments and will continue to do so until 2017, when revenues are projected to fall below benefit payments, after which the gap between expenditures and revenues continues to widen.

Income and Expenditures as a Percent of Taxable Payroll. Chart 3 shows annual income (excluding interest but including both payroll and benefit taxes) and expenditures expressed as percentages of taxable payroll, commonly referred to as the income rate and cost rate, respectively.

The OASDI cost rate is projected to increase rapidly and first exceeds the income rate in 2017, producing cashflow deficits thereafter. As described above, surpluses that occur prior to 2017 are "loaned" to the General Fund and accumulate, with interest, reserve spending authority for the trust fund. The reserve spending authority represents an obligation for the General Fund. Beginning in 2017, Social Security will start using interest credits to meet full benefit obligations. The Government will need to raise taxes, reduce benefits, increase borrowing from the public, and/or cut spending for other programs to meet its obligations to the trust fund. By 2041, the trust fund reserves (and thus reserve spending authority) are projected to be exhausted. Even if a trust fund's assets are exhausted, however, tax income will continue to flow into the fund. Present tax rates would be sufficient to pay 78 percent of scheduled benefits after trust fund exhaustion in 2041 and 75 percent of scheduled benefits in 2082.

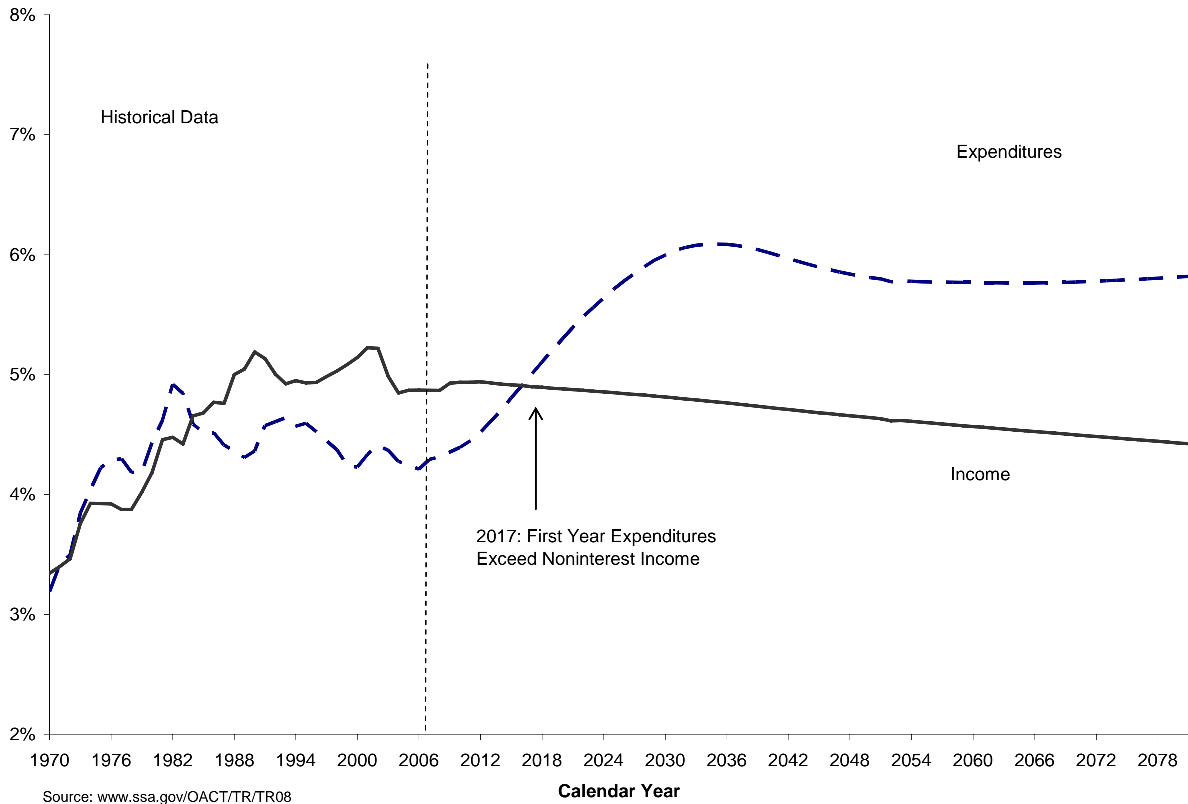
Chart 3—OASDI Income (Excluding Interest) and Expenditures as a Percent of Taxable Payroll 1970-2082



Source: www.ssa.gov/OACT/TR/TR08

Income and Expenditures as a Percent of Gross Domestic Product (GDP). Chart 4 shows estimated annual income (excluding interest) and expenditures, expressed as percentages of GDP, the total value of goods and services produced in the United States. This alternative perspective shows the size of the OASDI Program in relation to the capacity of the national economy to sustain it. The gap between expenditures and income generally widens with expenditures generally growing as a share of GDP and income declining slightly relative to GDP. Social Security's expenditures are projected to grow from 4.3 percent of GDP in 2008 to 5.8 percent in 2082. In 2082, expenditures are projected to exceed income by 1.4 percent of GDP.

Chart 4—OASDI Income (Excluding Interest) and Expenditures as a Percent of GDP 1970-2082



Sensitivity Analysis. Actual future income from OASDI payroll taxes and other sources and actual future expenditures for scheduled benefits and administrative expenses will depend upon a large number of factors: the size and composition of the population that is receiving benefits, the level of monthly benefit amounts, the size and characteristics of the work force covered under OASDI, and the level of workers' earnings. These factors will depend, in turn, upon future marriage and divorce rates, birth rates, death rates, migration rates, labor force participation and unemployment rates, disability incidence and termination rates, retirement age patterns, productivity gains, wage increases, cost-of-living increases, and many other economic and demographic factors.

This section presents estimates that illustrate the sensitivity of long-range expenditures and income for the OASDI Program to changes in *selected individual assumptions*. In this analysis, the intermediate assumption is used as the reference point, and one assumption at a time is varied. The variation used for each individual assumption reflects the levels used for that assumption in the low cost (Alternative I) and high cost (Alternative III) projections. For example, when analyzing sensitivity with respect to variation in real wages, income and expenditure projections using the intermediate assumptions are compared to the outcome when projections are done by changing only the real wage assumption to either low cost or high cost alternatives.

The low cost alternative is characterized by assumptions that generally improve the financial status of the program (relative to the intermediate assumption) such as slower improvement in mortality (beneficiaries die younger). In contrast, assumptions under the high cost alternative generally worsen the financial outlook. One exception occurs with the consumer price index (CPI) assumption (see below).

Table 2 shows the effects of changing individual assumptions on the present value of estimated OASDI expenditures in excess of income (the *shortfall* of income relative to expenditures in present value terms). The assumptions are shown in parentheses. For example, the intermediate assumption for the annual rate of *reduction in age-sex-adjusted death rates* is 0.75 percent. For the low cost alternative, a slower reduction rate (0.30 percent) is assumed as it means that beneficiaries die at a younger age relative to the intermediate assumption, resulting in lower expenditures. Under the low cost assumption, the shortfall drops from $6,555 billion to $4,885 billion, a 25 percent smaller shortfall. The high cost death rate assumption (1.26 percent) results in an increase in the shortfall, from $6,555 billion to $8,301 billion, a 27 percent increase in the shortfall. Clearly, alternative death rate assumptions have a substantial impact on estimated future cashflows in the OASDI Program.

A higher fertility rate means more workers relative to beneficiaries over the projection period, thereby lowering the shortfall relative to the intermediate assumption. An increase in the rate from 2.0 to 2.3 percent results in a 13 percent smaller shortfall (i.e., expenditures less income), from $6,555 billion to $5,702 billion.

Higher real wage growth results in faster income growth relative to expenditure growth. Table 2 shows that a real wage differential that is 0.5 greater than the intermediate assumption of 1.1 results in a drop in the shortfall from $6,555 billion to $5,324 billion, a 19 percent decline.

The CPI change assumption operates in a somewhat counterintuitive manner, as seen in Table 2. A lower rate of change results in a higher shortfall. This arises as a consequence of holding the real wage assumption constant while varying the CPI so that wages (the income base) are affected sooner than benefits. If the rate is assumed to be 1.8 percent rather than 2.8 percent, the shortfall rises about 7 percent, from $6,555 billion to $7,034 billion.

The effect of net immigration is similar to fertility in that, over the 75-year projection period, higher immigration results in proportionately more workers (taxpayers) than beneficiaries. The low-cost assumption for net immigration results in a 6 percent drop in the shortfall, from $6,555 billion to $6,141 billion, relative to the intermediate case; and the high-cost assumption results in a 6 percent higher shortfall.

Finally, Table 2 shows the sensitivity of the shortfall to variations in the real interest rate or, in present value terminology, the sensitivity to alternative discount rates assuming a higher discount rate results in a lower present value. The shortfall of $5,050 billion is 23 percent lower when the real interest rate is 3.6 percent rather than 2.9 percent, and 37 percent higher when the real interest rate is 2.1 percent rather than 2.9 percent.

Table 2
Present Values of Estimated OASDI Expenditures in Excess of Income under Various Assumptions, 2008-2082

(Dollar values in billions; values of assumptions shown in parentheses)

	Shortfall		
Assumption	Low	Intermediate	High
Average annual reduction in death rates ..	4,885 (0.30)	6,555 (0.75)	8,301 (1.26)
Total fertility rate	5,702 (2.3)	6,555 (2.0)	7,423 (1.7)
Real wage differential	5,324 (1.6)	6,555 (1.1)	7,452 (0.6)
CPI change	6,068 (3.8)	6,555 (2.8)	7,034 (1.8)
Net immigration	6,141 (1,375,000) [1]	6,555 (1,070,000) [1]	6,950 (790,000) [1]
Real interest rate	5,050 (3.6)	6,555 (2.9)	8,969 (2.1)

[1] Amounts represent the average annual net immigration over the 75-year projection period.

Source: 2008 OASDI Trustees Report and SSA.

Medicare Projections

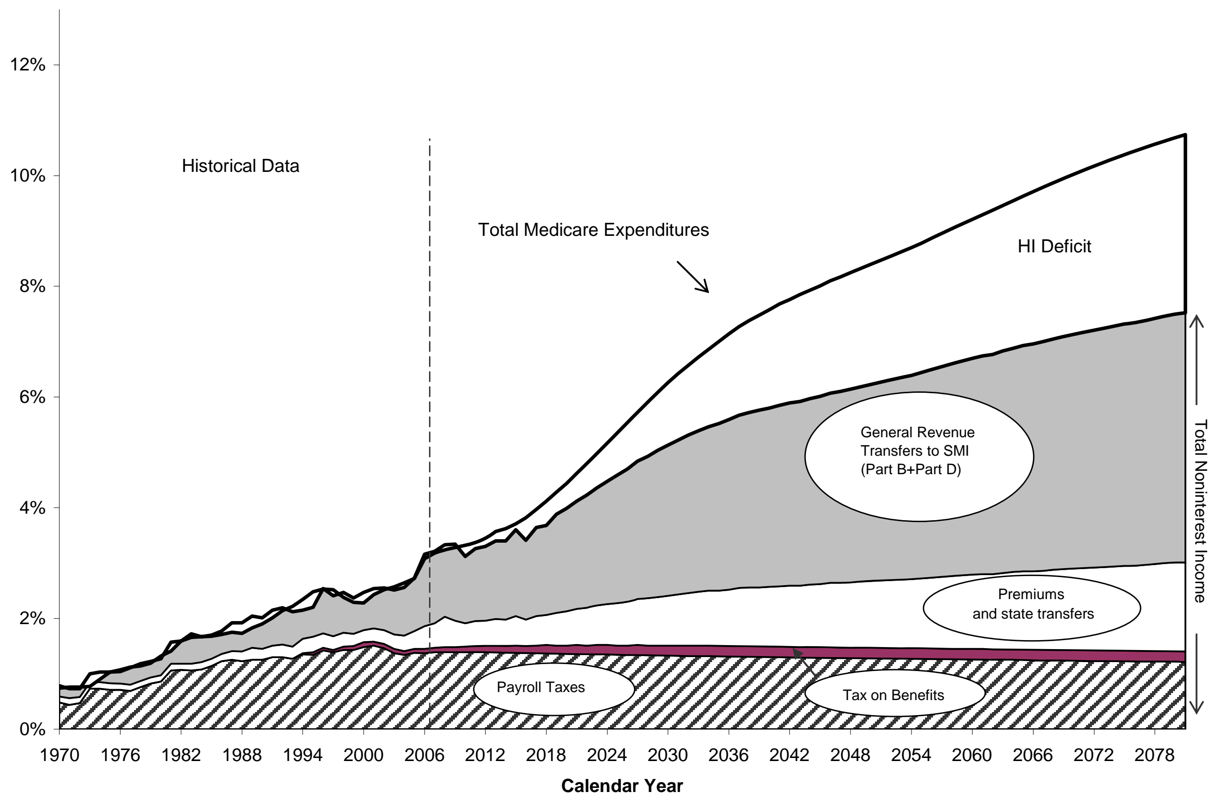
Medicare Legislation. On December 8, 2003, President Bush signed into law the Medicare Prescription Drug, Improvement, and Modernization Act of 2003. The 2003 law has a major impact on the operations and finances of Medicare. The law added a prescription drug benefit to Medicare beginning in 2006 and a new prescription drug account in the SMI Trust Fund. The benefit can be obtained through a private drug-only plan, a private preferred-provider organization or health maintenance organization, or through an employer-sponsored retiree health plan. The preferred-provider organizations are new to the Medicare Program and operate on a regional basis. The Government assumes some of the costs of providing prescription drug coverage to people eligible for both Medicare and Medicaid.

The legislation also includes provisions not related to the prescription drug benefit. It includes increases in Medicare provider reimbursements, higher Medicare Part B premiums for people at higher income levels, and an expansion of tax-deductible health savings accounts. The 2003 legislation is expected to have a significant effect on future Medicare finances as seen below and earlier in the Statement of Social Insurance.

Health Care Cost Growth. In addition to the growth in the number of beneficiaries per worker, the Medicare Program has the added pressure of expected growth in the use and cost of health care per person. Continuing development and use of new technology is expected to cause health care expenditures to grow faster than GDP in the long run. For the intermediate assumption, health care expenditures per beneficiary are assumed to grow, on average, about one percentage point faster than per capita GDP over the long range.

Total Medicare. It is important to recognize the rapidly increasing long-range cost of Medicare and the large role of general revenues and beneficiary premiums in financing the SMI Program. Chart 5 shows expenditures and current-law noninterest revenue sources for HI and SMI combined as a percentage of GDP. The total expenditure line shows Medicare costs rising to 10.8 percent of GDP by 2082. Revenues from taxes and premiums (including State transfers under Part D) are expected to increase from 2.0 percent of GDP in 2008 to 3.0 percent of GDP in 2082. Payroll tax income declines gradually as a percent of GDP as growth in the number of workers paying such taxes slows and wages as a portion of compensation declines, offset by higher premiums combined for Parts B and D of SMI as a percent of GDP. General revenue contributions for SMI, as determined by current law, are projected to rise as a percent of GDP from 1.3 percent to 4.5 percent over the same period. Thus, revenues from taxes and premiums (including State transfers) will fall substantially as a share of total noninterest Medicare income (from 61 percent in 2008 to 40 percent in 2082) while general revenues will rise (from 39 percent to 60 percent). The gap between total noninterest Medicare income (including general revenue contributions) and expenditures begins around 2010 and then steadily continues to widen, reaching 3.3 percent of GDP by 2082.

Chart 5—Total Medicare (HI and SMI) Expenditures and Noninterest Income as a Percent of GDP 1970-2082

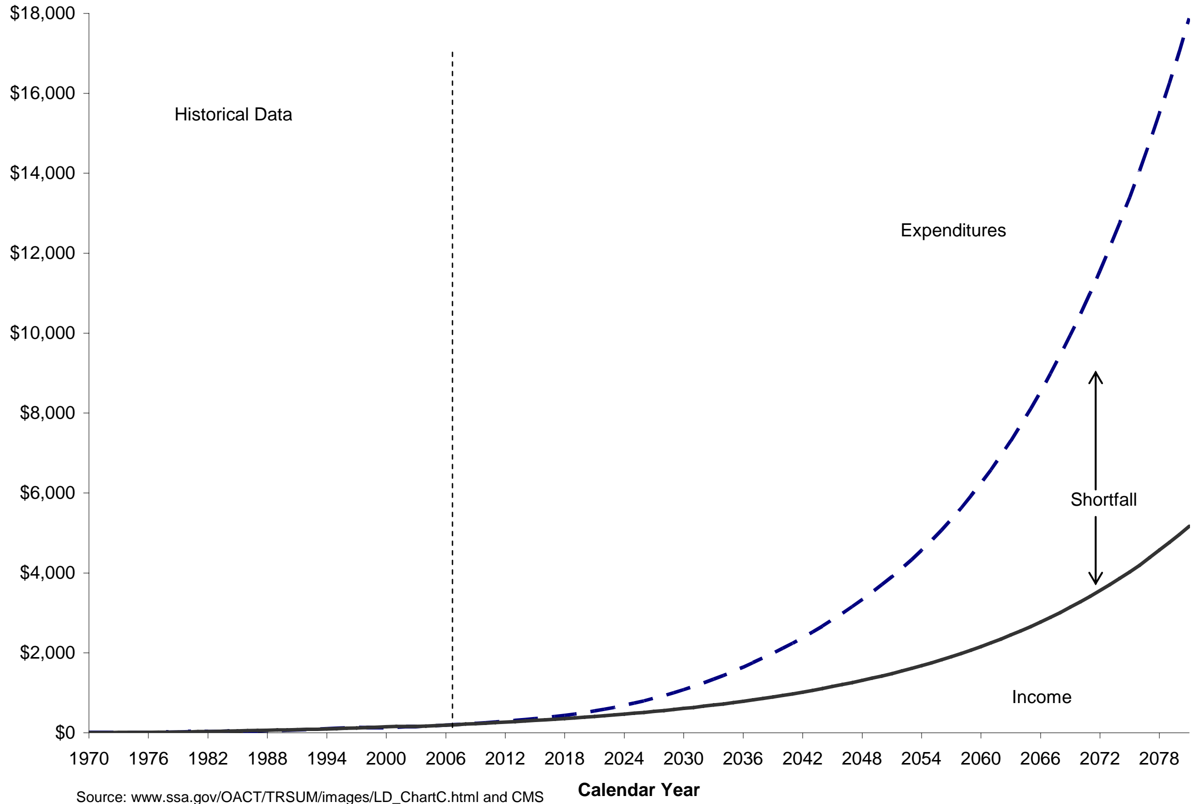


Source: www.ssa.gov/OACT/TRSUM/trsummary.html

Medicare, Part A (Hospital Insurance)─Nominal Income and Expenditures. Chart 6 shows historical and actuarial estimates of HI annual income (excluding interest) and expenditures for 1970-2082 in nominal dollars. The estimates are for the open-group population. The figure reveals a widening gap between projected income and expenditures.

Chart 6—Medicare Part A Income (Excluding Interest) and Expenditures 1970-2082

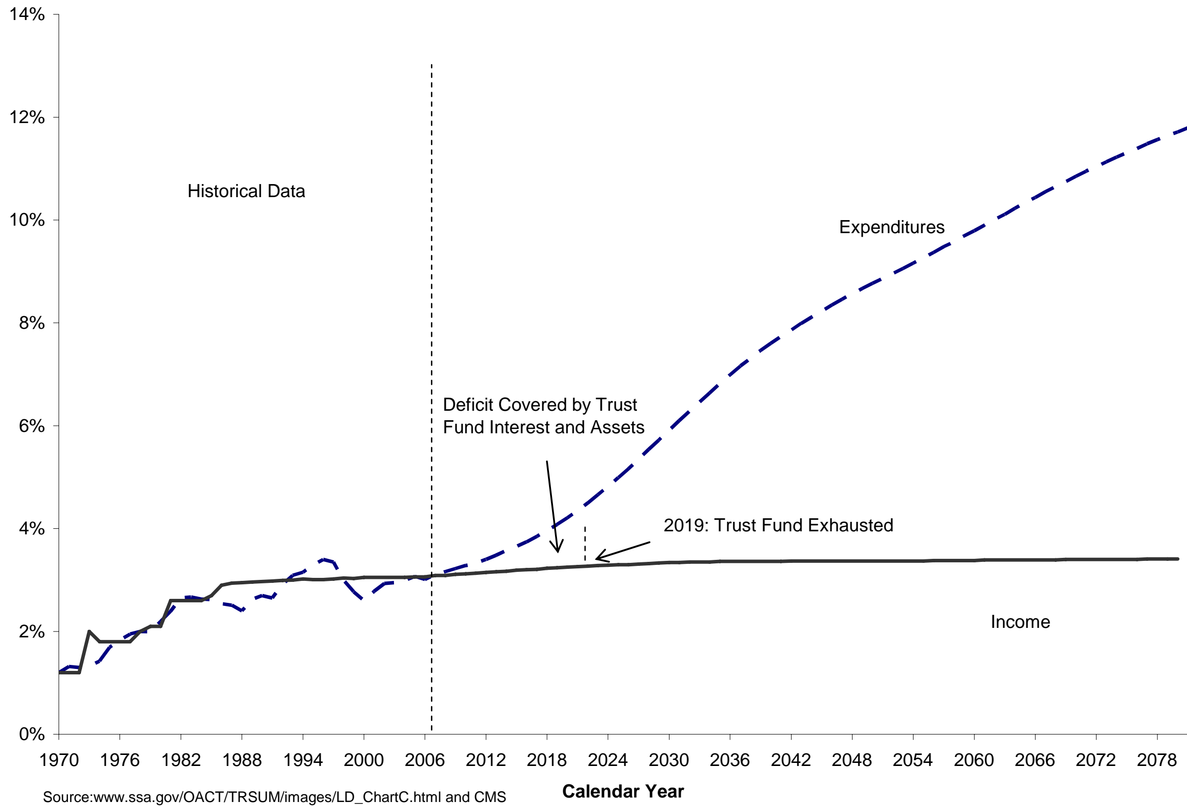
(In billions of nominal dollars)



Source: www.ssa.gov/OACT/TRSUM/images/LD_ChartC.html and CMS

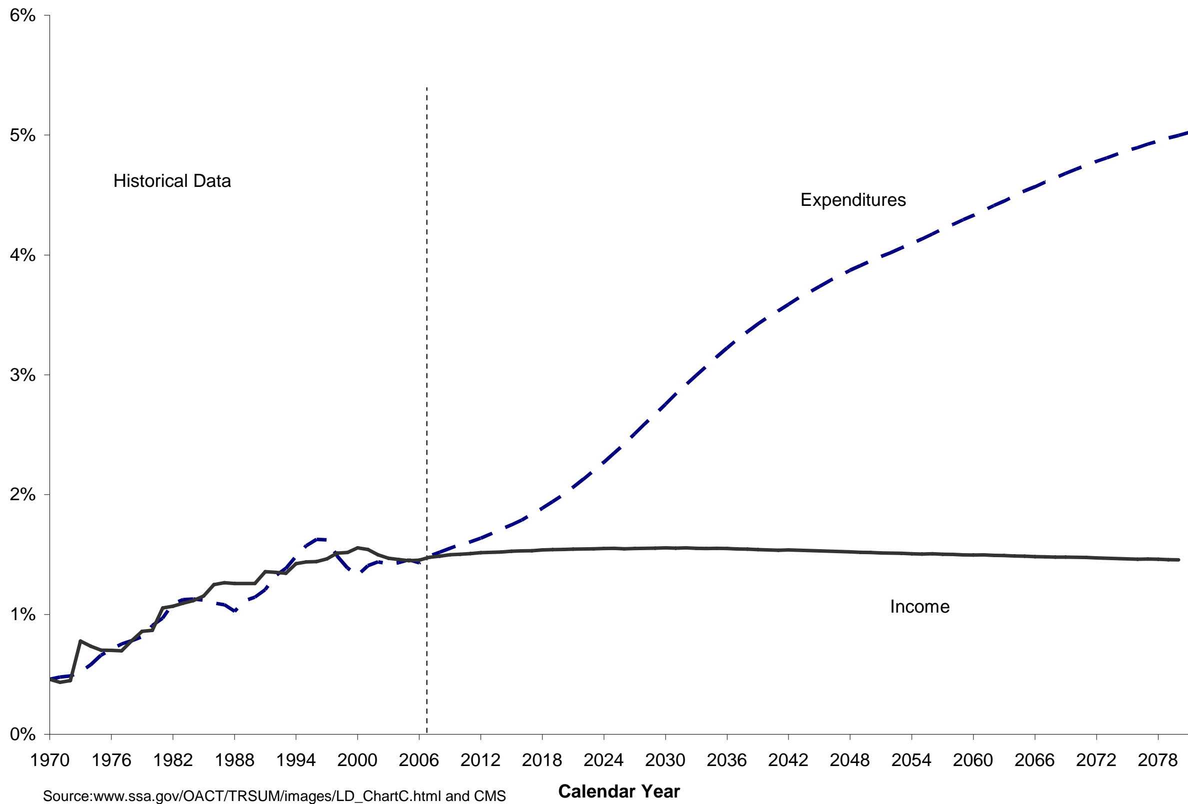
Medicare, Part A Income and Expenditures as a Percent of Taxable Payroll. Chart 7 illustrates income (excluding interest) and expenditures as a percentage of taxable payroll over the next 75 years. The chart shows that the expenditure rate exceeds the income rate in 2007, and cash deficits continue thereafter. Trust fund interest earnings and assets provide enough resources to pay full benefit payments until 2019 with general revenues used to finance interest and loan repayments to make up the difference between cash income and expenditures during that period. Pressures on the Federal budget will thus emerge well before 2019. Present tax rates would be sufficient to pay 78 percent of scheduled benefits after trust fund exhaustion in 2019 and 30 percent of scheduled benefits in 2082.

Chart 7—Medicare Part A Income (Excluding Interest) and Expenditures as a Percent of Taxable Payroll 1970-2082



Medicare Part A Income and Expenditures as a Percent of GDP. Chart 8 shows estimated annual income (excluding interest) and expenditures, expressed as percentages of GDP, the total value of goods and services produced in the United States. This alternative perspective shows the size of the HI Program in relation to the capacity of the national economy to sustain it. Medicare Part A's expenditures are projected to grow from 1.6 percent of GDP in 2008, to 2.7 percent in 2030, and to 4.8 percent by 2082. The gap between expenditures and income widens continuously with expenditures growing as a share of GDP and income declining slightly relative to GDP. By 2082, expenditures are projected to exceed income by 3.4 percent of GDP.

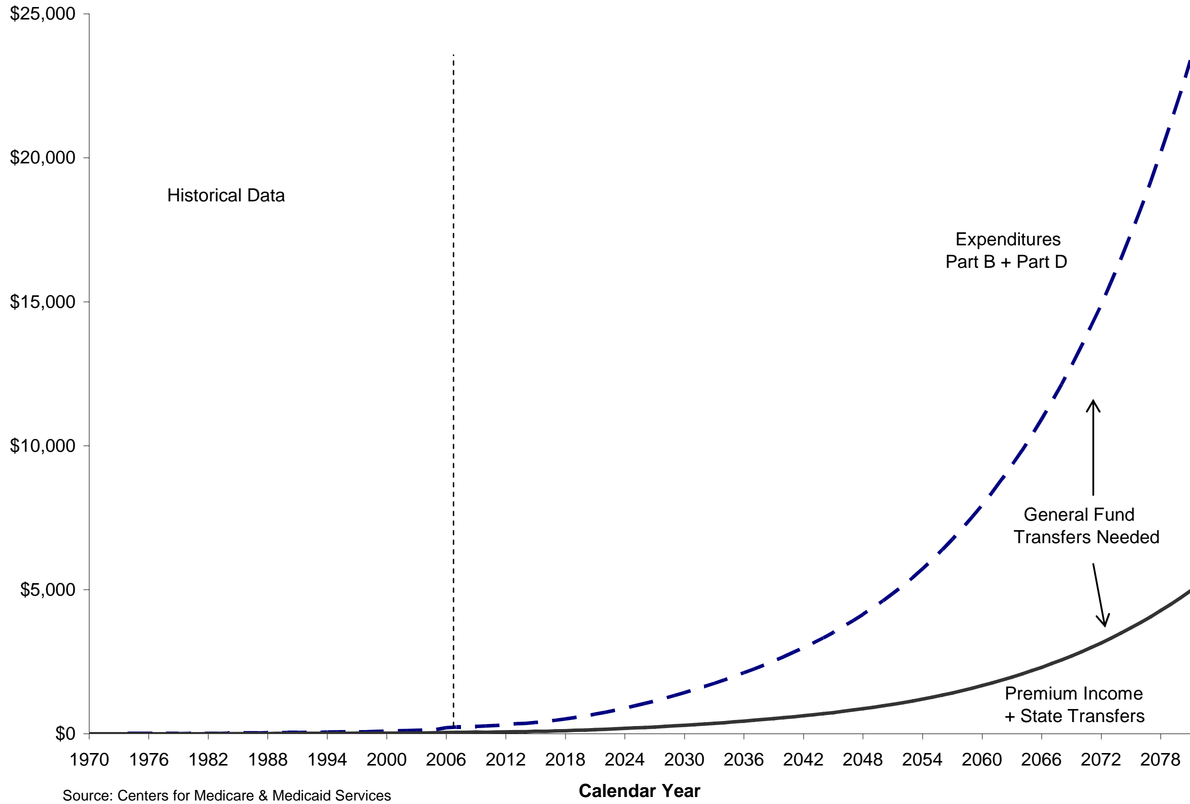
Chart 8—Medicare Part A Income (Excluding Interest) and Expenditures as a Percent of GDP 1970-2082



Medicare, Parts B and D (Supplementary Medical Insurance). Chart 9 shows historical and actuarial estimates of Medicare Part B and Part D premiums (and Part D State transfers) and expenditures for each of the next 75 years, in nominal dollars. The gap between premiums and State transfer revenues and program expenditures, a gap that will need to be filled with transfers from general revenues, grows throughout the projection period.

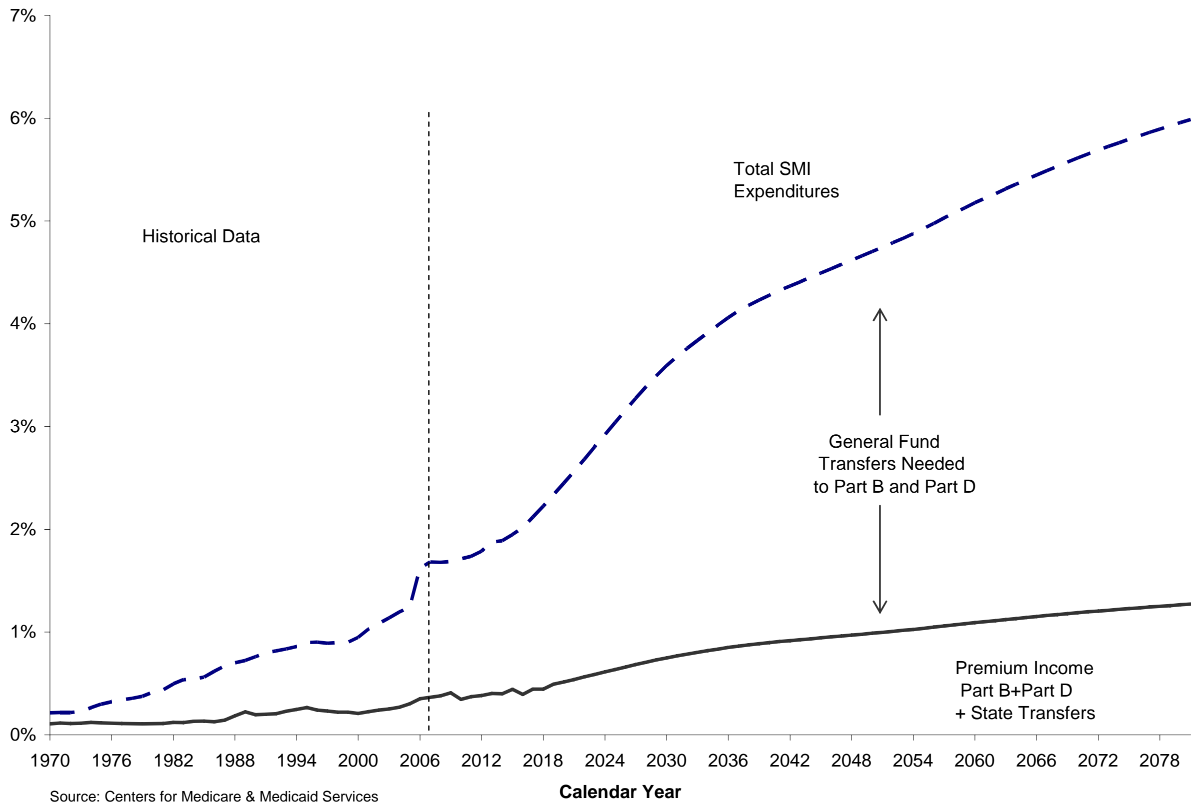
Chart 9—Medicare Part B and Part D Premium and State Transfer Income and Expenditures 1970-2082

(In billions of nominal dollars)



Medicare Part B and Part D Premium and State Transfer Income and Expenditures as a Percent of GDP. Chart 10 shows expenditures for the Supplementary Medical Insurance Program over the next 75 years expressed as a percentage of GDP, providing a perspective on the size of the SMI Program in relation to the capacity of the national economy to sustain it. In 2008, SMI expenditures are expected to be $242 billion or 1.7 percent of GDP. After 2008, this percentage is projected to increase steadily reaching 6.0 percent in 2082. This reflects growth in the volume and intensity of Medicare services provided per beneficiary throughout the projection period, including the prescription drug benefits, together with the effects of the baby boom retirement. Premium and State transfer income grows from about 0.4 percent in 2008 to 1.3 percent of GDP in 2082, so the portion financed by General Fund transfers to SMI is projected to be about 75 percent throughout the projection period.

Chart 10—Medicare Part B and Part D Premium and State Transfer Income and Expenditures as a Percent of GDP 1970-2082



Medicare Sensitivity Analysis. This section illustrates the sensitivity of long-range cost and income estimates for the Medicare Program to changes in *selected individual assumptions*. As with the OASDI analysis, the intermediate assumption is used as the reference point, and one assumption at a time is varied. The variation used for each individual assumption reflects the levels used for that assumption in the low cost and high cost projections (see description of sensitivity analysis for OASDI).

Table 3 shows the effects of changing various assumptions on the present value of estimated HI expenditures in excess of income (the *shortfall* of income relative to expenditures in present value terms). The assumptions are shown in parentheses. Clearly, net HI expenditures are extremely sensitive to alternative assumptions about the growth in health care cost. For the low cost alternative, the slower growth in health costs causes the shortfall to drop from $12,736 billion to $5,083 billion, a 60 percent smaller shortfall. The high cost assumption results in a near doubling of the shortfall, from $12,736 billion to $25,196 billion.

Variations in the next four assumptions in Table 3 result in relatively minor changes in net HI expenditures. The higher or lower fertility assumptions cause a less than 2 percent change in the shortfall relative to the intermediate case. The higher real wage growth rate results in about a 6 percent greater shortfall while a lower growth rate reduces the shortfall by about 8 percent. Wages are a key cost factor in the provision of health care. Higher wages also result in greater payroll tax income. HI expenditures exceed HI income by a wide and increasing margin in the future (Charts 6 to 8). As a result, an assumed higher real wage differential has a larger impact on HI expenditures than HI income, thereby increasing the shortfall of income relative to expenditures. CPI and net immigration changes have very little effect on net HI expenditures. Higher immigration increases the net shortfall modestly as higher payroll tax revenue is more than offset by higher medical care expenditures.

Table 3 also shows that the present value of net HI expenditures is 25 percent lower if the real interest rate is 3.6 percent rather than 2.9 percent and 41 percent higher if the real interest rate is 2.1 percent rather than 2.9 percent.

Table 3
Present Values of Estimated Medicare Part A Expenditures in Excess of Income Under Various Assumptions, 2008-2082

(Dollar values in billions; values of assumptions shown in parentheses)

	Shortfall		
Assumption[1]	**Low**	**Intermediate**	**High**
Average annual growth in health costs[2]	5,083 (3.1)	12,736 (4.1)	25,196 (5.1)
Total fertility rate[3]	12,499 (2.3)	12,736 (2.0)	12,980 (1.7)
Real wage differential	11,918 (1.6)	12,736 (1.1)	13,742 (0.6)
CPI change	12,669 (1.8)	12,736 (2.8)	12,744 (3.8)
Net immigration	12,658 (1,375,000)[4]	12,736 (1,070,000)[4]	13,062 (790,000)[4]
Real interest rate	9,599 (3.6)	12,736 (2.9)	17,936 (2.1)

[1] The sensitivity of the projected HI net cashflow to variations in future mortality rates is also of interest. At this time, however, relatively little is known about the relationship between improvements in life expectancy and the associated changes in health status and per beneficiary health expenditures. As a result, it is not possible at present to prepare meaningful estimates of the Part A, mortality sensitivity.
[2] Annual growth rate is the aggregate cost of providing covered health care services to beneficiaries. The low cost and high cost alternatives assume that costs increase 1 percent slower or faster, respectively, than the intermediate assumption, *relative to growth in taxable payroll.*
[3] The total fertility rate for any year is the average number of children who would be born to a woman in her lifetime if she were to experience the birth rates by age observed in, or assumed for, the selected year and if she were to survive the entire childbearing period.
[4] Amount represents the average annual net immigration over the 75-year projection period.

Table 4 shows the effects of various assumptions about the growth in health care costs on the present value of estimated SMI (Medicare Parts B and D) expenditures in excess of income. As with HI, net SMI expenditures are very sensitive to changes in the health care cost growth assumption. For the low cost alternative, the slower assumed growth in health costs reduces the Governmentwide resources needed for Part B from $15,719 billion to $10,984 billion and in Part D from $7,857 billion to $5,468 billion, about a 30 percent difference in each case. The high-cost assumption increases Governmentwide resources needed to $23,260 billion for Part B and to $11,650 billion for Part D, about a 48 percent difference in each case.

Table 4
Present Values of Estimated Medicare Parts B and D Future Expenditures Less Premium Income and State Transfers Under Three Health Care Cost Growth Assumptions, 2008-2082

(In billions of dollars)

Medicare Program[1]	Governmentwide Resources Needed		
	Low (4.1)	Intermediate (5.1)	High (6.1)
Part B	10,984	15,719	23,260
Part D	5,468	7,857	11,650

[1] Annual growth rate is the aggregate cost of providing covered health care services to beneficiaries. The low and high scenarios assume that costs increase one percent slower or faster, respectively, than the intermediate assumption.

Source: Centers for Medicare & Medicaid Services.

Sustainability of Social Security and Medicare

75-Year Horizon

According to the 2008 Medicare Trustees Report, the HI Trust Fund is projected to remain solvent until 2019 and, according to the 2008 Social Security Trustees Report, the OASDI Trust Funds are projected to remain solvent until 2041. In each case, some general revenues must be used to satisfy the authorization of full benefit payments until the year of exhaustion. This occurs when the trust fund balances accumulated during prior years are needed to pay benefits, which leads to a transfer from general revenues to the trust funds. Moreover, under current law, General Fund transfers to the SMI Trust Fund will occur into the indefinite future and will continue to grow with the growth in health care expenditures.

The potential magnitude of future financial obligations under these three social insurance programs is therefore important from a unified budget perspective as well as for understanding generally the growing resource demands of the programs on the economy. A common way to present future cashflows is in terms of their *present value*. This approach recognizes that a dollar paid or collected next year is worth less than a dollar today, because a dollar today could be saved and earn a year's worth of interest (see footnote 1).

Table 5 shows the magnitudes of the primary expenditures and sources of financing for the three trust funds computed on an open-group basis for the next 75 years and expressed in present values. The data are consistent with the Statements of Social Insurance included in the principal financial statements. For HI, revenues from the public are projected to fall short of total expenditures by $12,736 billion in present value terms which is the additional amount needed in order to pay scheduled benefits over the next 75 years. [5] From the trust fund perspective, the amount needed is $12,424 billion in present value after subtracting the value of the existing trust fund balances (an asset to the trust fund account but an intragovernmental transfer to the overall budget). For SMI, revenues from the

[5] Interest income is not a factor in this table as dollar amounts are in present value terms.

public for Parts B and D combined are estimated to be $23,576 billion[6] less than total expenditures for the two accounts, an amount that, from a budget perspective, will be needed to keep the SMI program solvent for the next 75 years. From the trust fund perspective, however, the present values of total revenues and total expenditures for the SMI Program are roughly equal due to the annual adjustment of revenue from other Government accounts to meet program costs.[7] For OASDI, projected revenues from the public fall short of total expenditures by $6,555 billion[8] in present value dollars and, from the trust fund perspective, by $4,317 billion.

From the Governmentwide perspective, the present value of the total resources needed for the Social Security and Medicare Programs equals $42,867 billion, in addition to payroll taxes, benefit taxes, and premium payments from the public. From the trust fund perspective, which counts the trust funds and the general revenue transfers to the SMI Program as dedicated funding sources additional resources in the amount of $16,685 billion in present value terms are needed, beyond the $23,576 billion in present value of required general revenue transfers already scheduled for the SMI Program and the $2,606 billion to honor the trust fund investments in Treasury securities.

Table 5
Present Values of Costs Less Revenues of 75-Year Open Group Obligations HI, SMI, and OASDI

(In billions of dollars, as of January 1, 2008)

		SMI			
	HI	**Part B**	**Part D**	**OASDI**	**Total**
Revenues from the public:					
Taxes	11,883	-	-	36,357	48,240
Premiums, State transfers	-	5,478	2,107	-	7,585
Total	11,883	5,478	2,107	36,357	55,825
Total costs to the public	24,619	21,197	9,964	42,911	98,691
Net results for Government-wide (budget) perspective*	12,736	15,719	7,857	6,555	42,867
Revenues from other Government accounts	-	15,719	7,857	-	23,576
Trust fund as of 1/1/2008	312	53	3	2,238	2,606
Net results for trust fund perspective*	12,424	(53)	(3)	4,317	16,685

*Net results are computed as costs less revenues.

Note: Details may not add to totals due to rounding.

Source: 2008 OASDI and Medicare Trustees' Reports.

[6] For 2008, the present value of estimated future expenditures in excess of estimated future revenue for the Part B program increased $2,287 billion as compared to that reported for 2007. This growth is primarily attributable to (1) the significant increase in the residual growth rate (the per capita growth in medical costs over the growth in gross domestic product) for the intermediate years of the projection period (i.e., for 2018 through 2031), and (2) the normal annual level of increase including interest in moving the 75-year projection period year forward from the prior year's valuation date (i.e., where much larger amounts of estimated future expenditures in excess of future revenues associated with the last year of the current year's projection period replaced smaller amounts of estimated future expenditures in excess of future revenue associated with the first year of the prior year's projection period). For 2008, the present value of estimated future expenditures in excess of estimated future revenue for the Part D program decreased $504 billion as compared to that reported for 2007. This reduction is primarily attributable to actual experience in 2006 where actual drug costs were much lower than expected, while manufacturer rebates were greater than anticipated. In addition, the projected trend for the next few years, which is based on the projected growth in prescription drug spending nationally, is lower than in the prior year's projections.

[7] The SMI Trust Fund also has a very small amount of existing assets.

[8] For 2007, the present value of future expenditures exceeded future revenue by $6,763 billion. The improvement in the long-range acturial status of the OASDI program indicated in this report is principally the result of changes in immigration methods and assumptions. These changes resulted in substantial reductions in the projected cost of the program as a percentage of taxable payroll, particularly in the latter half of the long-range projection period.

Infinite Horizon

The 75-year horizon represented in Table 5 is consistent with the primary focus of the Social Security and Medicare Trustees' Reports. For the OASDI Program, for example, an additional $6.6 trillion in present value will be needed above currently scheduled taxes to pay for scheduled benefits ($4.3 trillion from the trust fund perspective). Yet, a 75-year projection is not a complete representation of all future financial flows through the infinite horizon. For example, when calculating unfunded obligations, a 75-year horizon includes revenue from some future workers but only a fraction of their future benefits. In order to provide a more complete estimate of the long-run unfunded obligations of the programs, estimates can be extended to the infinite horizon. The open-group infinite horizon net obligation is the present value of all expected future program outlays less the present value of all expected future program tax and premium revenues. Such a measure is provided in Table 6 for the three trust funds represented in Table 5.

From the budget or Governmentwide perspective, the values in line 1 plus the values in line 4 of Table 6 represent the value of resources needed to finance each of the programs into the infinite future. The sums are shown in the last line of the table (also equivalent to adding the values in the second and fifth lines). The total resources needed for all the programs sums to more than $101 trillion in present value terms. This need can be satisfied only through increased borrowing, higher taxes, reduced program spending, or some combination.

The second line shows the value of the trust fund at the beginning of 2008. For the HI and OASDI Programs this represents, from the trust fund perspective, the extent to which the programs are funded. From that perspective, when the trust fund is subtracted, an additional $34.4 trillion and $13.7 trillion, respectively, are needed to sustain the programs into the infinite future. As described above, from the trust fund perspective, the SMI Program is fully funded. The substantial gap that exists between premiums and State transfer revenue and program expenditures in the SMI Program ($33.9 trillion + $17.2 trillion) represents future general revenue obligations of the Federal budget.

In comparison to the analogous 75-year number in Table 5, extending the calculations beyond 2082, captures the full lifetime benefits and taxes and premiums of all current and future participants. The shorter horizon understates financial needs by capturing relatively more of the revenues from current and future workers and not capturing all of the benefits that are scheduled to be paid to them.

Table 6
Present Values of Costs Less Tax, Premium and State Transfer Revenue through the Infinite Horizon, HI, SMI, OASDI

(In trillions of dollars as of January 1, 2008)

		SMI			
	HI	Part B	Part D	OASDI	Total
Present value of future costs less future taxes and premiums and State transfers for current participants	13.6	12.6	5.6	17.4	49.2
Less current trust fund	0.3	0.1	-	2.2	2.6
Equals net obligations for past and current participants	13.3	12.5	5.6	15.2	46.6
Plus net obligations for future participants	21.1	21.4	11.6	(1.5)	52.6
Equals net obligations through the infinite future for all participants	34.4	33.9	17.2	13.7	99.2
Present value of future costs less the present values of future income over the infinite horizon	34.7	34.0	17.2	15.9	101.8

Details may not add to totals due to rounding.

Source: 2008 OASDI and Medicare Trustees' Reports.

Railroad Retirement, Black Lung, and Unemployment Insurance

Railroad Retirement

The Railroad Retirement Board (RRB) was created in the 1930s to establish a retirement benefit program for the nation's railroad workers. As the Social Security Program legislated in 1935 would not give railroad workers credit for service performed prior to 1937, legislation was enacted in 1934, 1935, and 1937 (collectively the Railroad Retirement Acts of the 1930s) to establish a railroad retirement program separate from the Social Security Program.

Railroad retirement pays full retirement annuities at age 60 to railroad workers with 30 years of service. The program pays disability annuities based on total or occupational disability. It also pays annuities to spouses, divorced spouses, widow(er)s, remarried widow(er)s, surviving divorced spouses, children, and parents of deceased railroad workers. Medicare covers qualified railroad retirement beneficiaries in the same way as it does Social Security beneficiaries.

Payroll taxes paid by railroad employers and their employees provide a primary source of income for the Railroad Retirement and Survivors' Benefit Program. By law, railroad retirement taxes are coordinated with Social Security taxes. Employees and employers pay tier I taxes at the same rate as Social Security taxes. Tier II taxes finance railroad retirement benefit payments that are higher than Social Security levels.

Other sources of program income include: financial interchanges with the Social Security and Medicare trust funds, earnings on investments, Federal income taxes on railroad retirement benefits, and appropriations (provided after 1974 as part of a phase out of certain vested dual benefits). Refer to Note 23—Social Insurance, for additional information on railroad retirement program financing.

The Railroad Retirement and Survivors Improvement Act of 2001 (RRSIA) liberalized benefits for 30-year service employees and their spouses, eliminated a cap on monthly benefits for retirement and disability benefits, lowered minimum service requirements from 10 to 5 years, and provided for increased benefits for widow(er)s. Per the RRSIA, amounts in the Railroad Retirement Account and the Social Security Equivalent Benefit (SSEB) Account that are not needed to pay current benefits and administrative expenses are transferred to the National Railroad Retirement Investment Trust (NRRIT) whose sole purpose is to manage and invest railroad retirement assets. NRRIT's Board of Trustees is empowered to invest trust assets in nongovernmental assets, such as equities and debt, as well as, in Government securities. Prior to RRSIA, all investments were limited to Government securities.

Since its inception, NRRIT has received $21.3 billion from RRB (including $19.2 billion in fiscal year 2003, pursuant to RRSIA) and returned $6.3 billion. During fiscal year 2008, the NRRIT made net transfers of $1.3 billion to the RRB to pay retirement benefits. Administrative expenses of the trust are paid out of trust assets. The balance as of September 30, 2008, and 2007, of non-Federal securities and investments of the NRRIT are disclosed in Note 7—Securities and Investments.

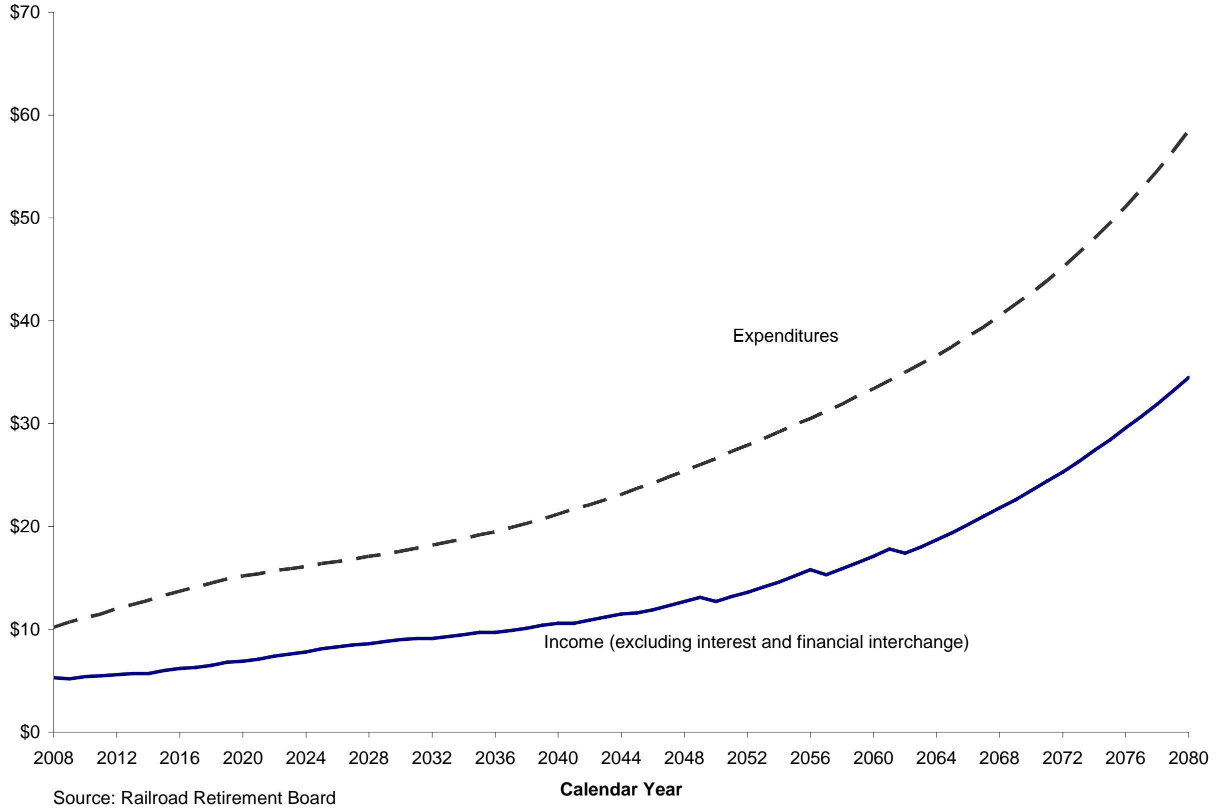
Cashflow Projections

Economic and Demographic Assumptions. The economic and demographic assumptions used for the most recent set of projections are shown in the "Railroad Retirement" section of Note 23—Social Insurance.

Nominal Income and Expenditures. Chart 11 shows, in nominal dollars, estimated railroad retirement income (excluding interest and financial interchange income) and expenditures for the period 2008-2082 based on the intermediate set of assumptions used in the RRB's actuarial evaluation of the program. The estimates are for the open-group population, which includes all persons projected to participate in the Railroad Retirement Program as railroad workers or beneficiaries during the period. Thus, the estimates include payments from, and on behalf of, those who are projected to be employed by the railroads during the period as well as those already employed at the beginning of the period. They also include expenditures made to, and on behalf of, such workers during that period.

Chart 11—Estimated Railroad Retirement Income (Excluding Interest and Financial Interchange Income) and Expenditures 2008-2082

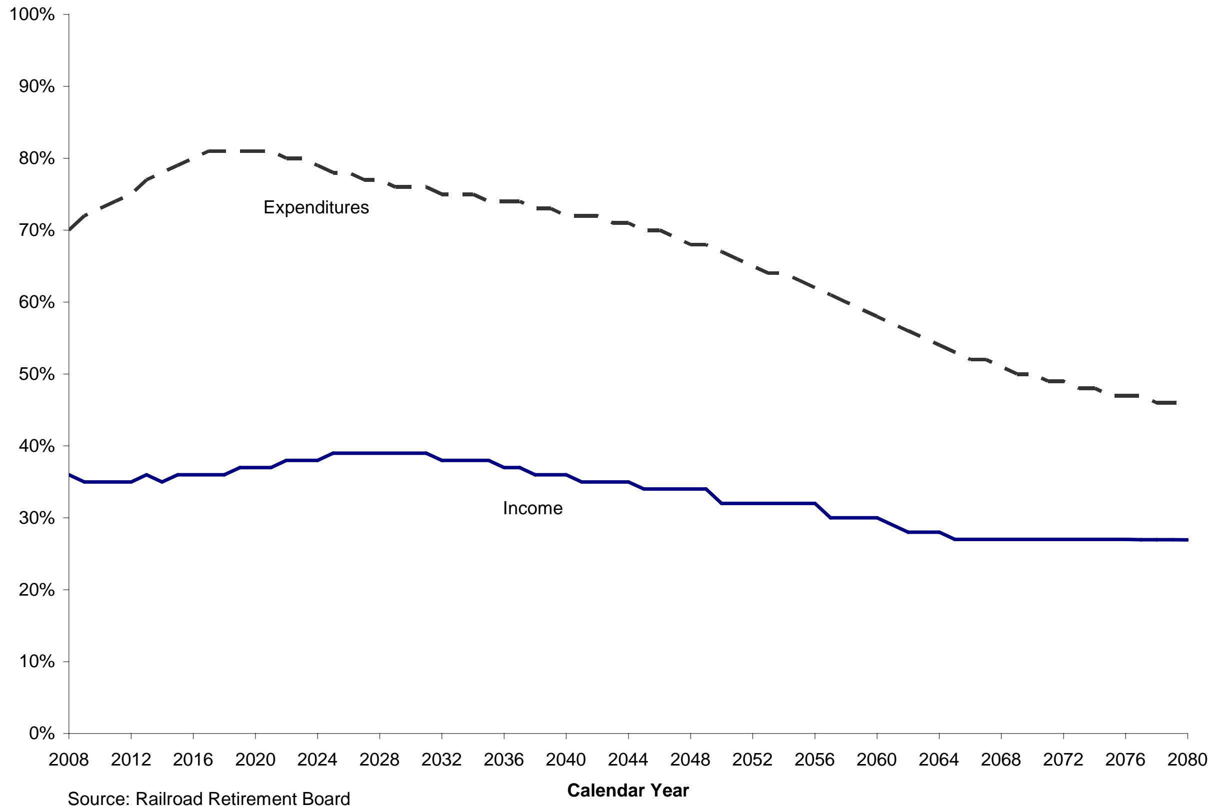
(In billions of nominal dollars)



As Chart 11 shows, expenditures are expected to exceed tax income for the entire projection period. The imbalances continue to widen until about 2020, hold steady for the next 15 years, and begin to grow steadily after 2035.

Income and Expenditures as a Percent of Taxable Payroll. Chart 12 shows estimated expenditures and income as a percent of tier II taxable payroll. The imbalances grow until 2017 but then begin to decrease steadily as expenditures fall. Tax rates begin to decline after 2032, stabilizing after 2064. Compared to last year, projected tax rates are slightly lower, on average. The tier II tax rate is determined from a tax rate table based on the average account benefit ratio.

Chart 12—Estimated Railroad Retirement Income (Excluding Interest and Financial Interchange Income) and Expenditures as a Percent of Tier II Taxable Payroll 2008-2082



Source: Railroad Retirement Board

Sensitivity Analysis. Actual future income from railroad payroll taxes and other sources and actual future expenditures for scheduled benefits and administrative expenses will depend upon a large number of factors as mentioned above. Two crucial assumptions are employment growth and the interest rate. Table 7 shows the sensitivity of the shortfall in the Railroad Retirement Program to variations in these two assumptions. The low-cost employment scenario has a 4.3 percent smaller shortfall of income to expenditures, and the high-cost scenario has a 3.5 percent higher shortfall. A higher discount rate reduces future values relative to a lower rate. As seen in the table, the shortfall is 30.1 percent lower if the interest rate is 11 percent rather than 7.5 percent and 72.8 percent higher when the interest rate is 4 percent rather than 7.5 percent.

Table 7
Present Values of Railroad Retirement Expenditures in Excess of Income Under Various Employment and Interest Rate Assumptions

(Dollar values in billions; values of assumptions shown in parentheses)

Assumption	Low	Middle	High
Employment[1]	104.6 (1.0%)	109.3 (2.5%)	113.1 (4.0%)
Interest rate...................	76.4 (11%)	109.3 (7.5%)	188.9 (4%)

[1] The low and middle employment scenarios have passenger service employment remaining at 43,000 workers per year and the remaining employment base declining at 1.0 percent and 2.5 percent, respectively, for the next 25 years. The high cost scenario has passenger service employment declining by 500 per workers per year until a level of 35,000 is reached with the remaining employment base declining by 4.0 percent per year for 25 years, at a reducing rate over the next 25 years, and remaining level thereafter.

Source: Railroad Retirement Board.

Sustainability of Railroad Retirement

Table 8 shows the magnitudes of the primary expenditures and sources of financing for the Railroad Retirement Program computed on an open-group basis for the next 75 years and expressed in present values as of January 1, 2008. The data are consistent with the Statements of social Insurance.

From a Governmentwide perspective, revenues are expected to fall short of expenditures by approximately $109.3 billion, which represents the present value of resources needed to sustain the Railroad Retirement Program. From a trust fund perspective, when the trust fund balance and the financial interchange and transfers are included, the combined balance of the NRRIT, the Railroad Retirement Account, and the SSEB Account show a slight surplus.

Table 8
Present Values of 75-Year Projections of Revenues and Expenditures for the Railroad Retirement Program[1, 2]

(In billions of present-value dollars as of January 1, 2008)

Estimated future income (excluding interest)[3] received from or on behalf of:	
Current participants who have attained retirement age	4.9
Current participants not yet having attained retirement age	42.8
Those expected to become participants	54.4
All participants	102.1
Estimated future expenditures:[4]	
Current participants who have attained retirement age	97.0
Current participants not yet having attained retirement age	88.4
Those expected to become participants	26.0
All participants	211.4
Net obligations from budget perspective (expenditures less income)	109.3
Railroad retirement program assets (mostly investments stated at market)[5]	33.2
Financial interchange from Social Security Trust	77.0
Net obligations from trust fund perspective	(0.9)

[1] Represents combined values for the Railroad Retirement Account, SSEB Account, and NRRIT, based on middle employment assumption.
[2] The data used reflect the provisions of RRSIA of 2001.
[3] Future income (excluding interest) includes tier I taxes, tier II taxes, and income taxes on benefits.
[4] Future expenditures include benefits and administrative expenditures.
[5] The value of the fund reflects the 7.5 percent interest rate assumption. The RRB uses the relatively high rate due to investments in private securities.

Note: Detail may not add to totals due to rounding. Employee and beneficiary status are determined as of 1/1/2007 whereas present values are as of 1/1/2008.

Black Lung

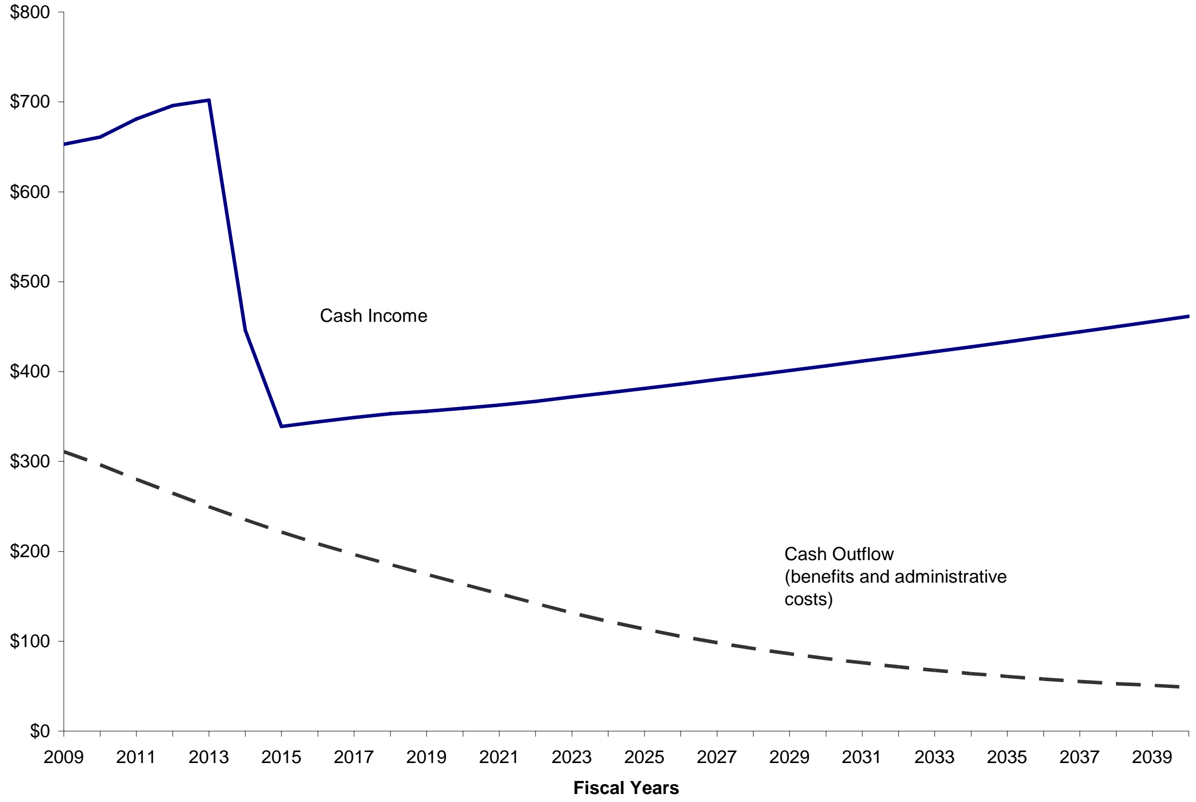
The Federal Coal Mine Health and Safety Act of 1969 created the Black Lung Disability Benefit Program to provide compensation and medical benefits for eligible coal miners who are disabled due to pneumoconiosis (black lung disease) arising out of their coal mine employment. The Department of Labor (DOL) operates the Black Lung Disability Benefit Program. The 1977 Black Lung Amendments established a Black Lung Disability Trust Fund (BLDTF) to provide benefit payments to eligible coal miners disabled by pneumoconiosis when no responsible mine operator can be assigned the liability. The beneficiary population has been declining as the incidence of black lung disease has fallen, and the group of miners affected by the disease (and their widows) has been dying at a more rapid rate than new awards have been made.

Excise taxes on coal mine operators, based on the sale of coal, is the primary source of financing black lung disability payments and related administrative costs. The Black Lung Benefits Revenue Act provides for repayable advances to the BLDTF from the General Fund of the Treasury in the event that BLDTF resources are not adequate to meet program obligations. On September 30, 2008, total liabilities of the BLDTF exceed assets by $10.4 billion. This deficit fund balance represents the accumulated shortfall of excise taxes necessary to meet benefit payment and interest expenses. This shortfall was funded by repayable advances to the BLDTF which are repayable with interest. Estimates for future interest on advances are based on the interest rates on outstanding advances ranging from 4.3 percent to 13.9 percent and new borrowings ranging from 4.9 percent to 5.6 percent.

From the budget or consolidated financial perspective, Chart 13 shows projected black lung expenditures (excluding interest) and excise tax collections for the period 2009-2040. The significant assumptions used in the most recent set of projections are shown in the “Black Lung” section of Note 23—Social Insurance. Analysts project that a scheduled reduction in taxes on coal sales will decrease cash inflows by 51 percent between the years 2013 to 2015. After 2015, cash surpluses widen due to a declining beneficiary population and increasing revenues. However, the picture dramatically changes when including projected interest payments that the program must make. Please see Note 25─Subsequent Events for more information.

Chart 13—Estimated Black Lung Income and Expenditures (Excluding Interest) 2009-2040

(In millions of nominal dollars)



Source: Department of Labor

Chart 14 shows the projected financial status of the program from a trust fund perspective that includes interest outflows from the program to the General Fund. Trust fund net outflows (benefits plus interest payments less cash income from excise taxes) grow without bound, as a result of projected interest payments on the large accumulated liability to the General Fund. This deficit fund balance represents the accumulated shortfall between excise taxes and benefit payment plus interest expenses.

Chart 14—Estimated Black Lung Trust Fund Net Outflow and End of Year Fund Balance 2009-2040

(In millions of nominal dollars)

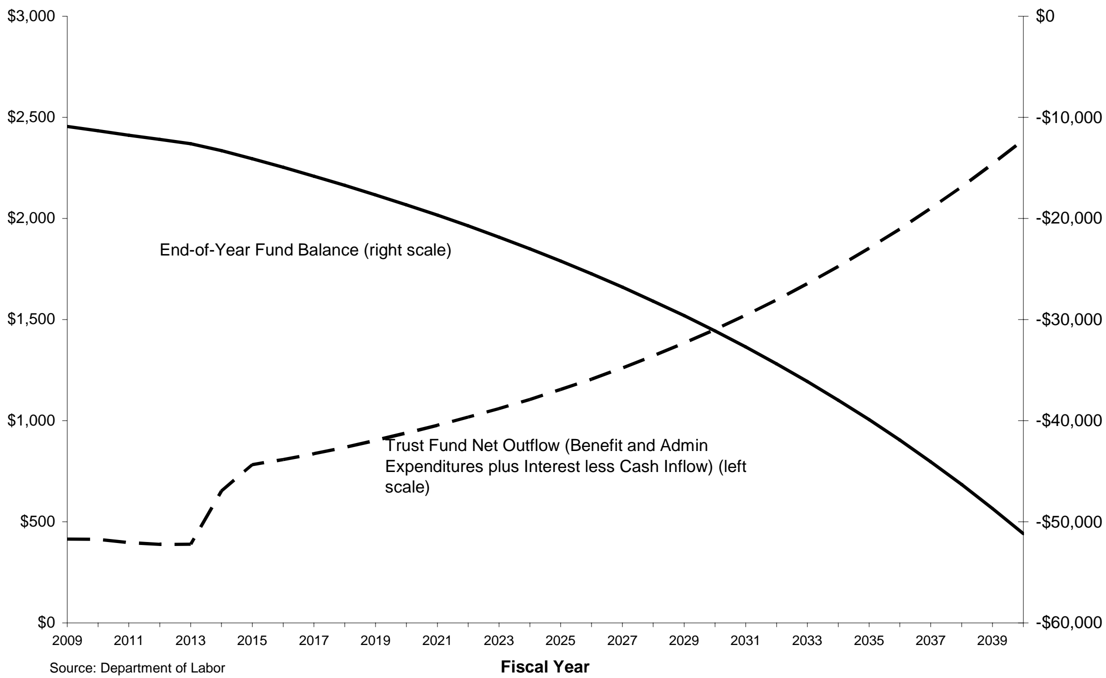


Table 9 shows present values of 32-year projections of expenditures and revenues for the Black Lung Program computed as of September 30, 2008, using a discount rate equivalent to 6.18 percent. (The discount rate is higher than the current Government borrowing rate because the program borrowed from the General Fund during periods of relatively high interest rates). From a Governmentwide (budget) perspective, the present value of expenditures is expected to be less than the present value of income by $4.0 billion (a surplus). From a trust fund perspective, a large balance ($10.4 billion) is owed to the General Fund. From that perspective, when that accumulated balance is combined with the cashflow surplus, the program shows a negative balance of $6.4 billion in present value dollars.

As a consequence of the Energy Improvement and Extension Act of 2008 that permitted restructuring of the debt of the Black Lung Disability Trust Fund (as well as an extension of higher excise taxes) the financial status of the fund is expected to be much improved (see Note 25—Subsequent Events). This will be reflected in future Financial Reports, beginning with the 2009 report.

Table 9
Present Values of 32-Year Projections of Revenues and Expenditures for the Black Lung Program

(In billions of present value dollars, as of September 30, 2008)

Estimated future tax income	6.5
Estimated future expenditures	2.5
Net obligations from budget perspective (expenditures less income)	(4.0)
Accumulated balance due general fund	10.4
Net obligations from trust fund perspective	6.4

Note: Detail may not add to totals due to rounding.

Source: Department of Labor projections and Treasury Department calculations.

Unemployment Insurance

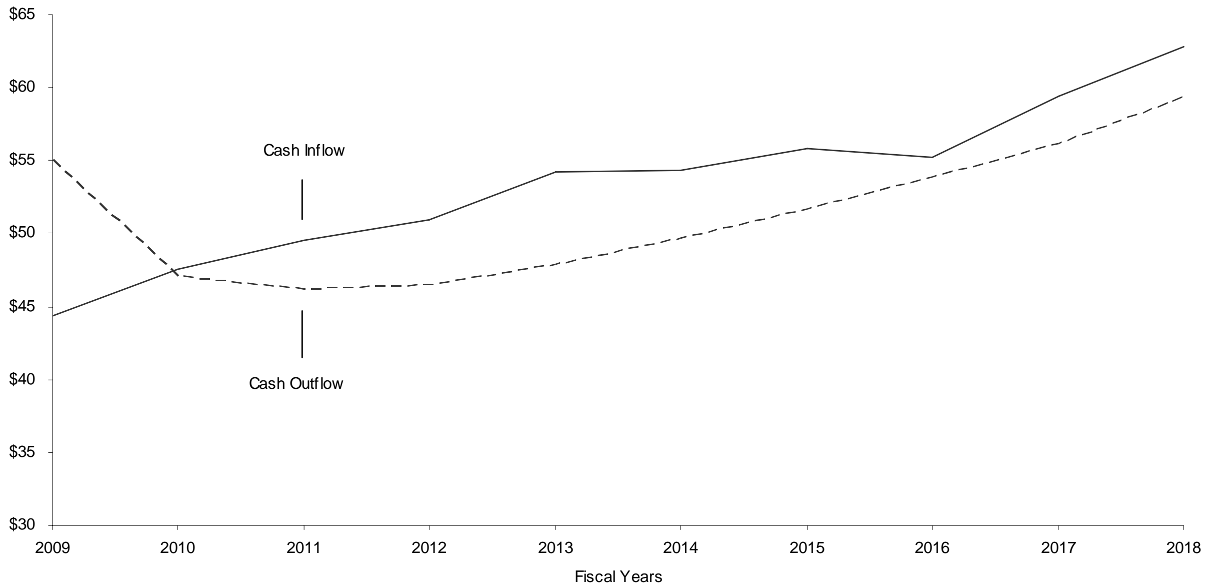
The Unemployment Insurance Program was created in 1935 to provide temporary partial wage replacement to workers who lost their jobs. The program is administered through a unique system of Federal and State partnerships established in Federal law but administered through conforming State laws by State agencies. DOL interprets and enforces Federal law requirements and provides broad policy guidance and program direction, while program details such as benefit eligibility, duration, and amount of benefits are established through individual State unemployment insurance statutes and administered through State unemployment insurance agencies.

The program is financed through the collection of Federal and State unemployment taxes that are credited to the Unemployment Trust Fund (UTF) and reported as Federal tax revenue. The fund was established to account for the receipt, investment, and disbursement of unemployment taxes. Federal unemployment taxes are used to pay for Federal and State administration of the Unemployment Insurance Program, veterans' employment services, State employment services, and the Federal share of extended unemployment insurance benefits. Federal unemployment taxes are also used to maintain a loan account within the UTF, from which insolvent State accounts may borrow funds to pay unemployment insurance benefits.

Chart 15 shows the projected cash contributions and expenditures over the next 10 years under expected economic conditions (described below). The significant assumptions used in the projections include total unemployment rates, civilian labor force levels, percent of unemployed receiving benefits, total wages, distribution of benefit payments by State, State tax rate structures, State taxable wage bases, and interest rates on UTF investments. These projections, excluding interest earnings indicate a negative net cash flow in 2009 followed by positive net cash flow for the remainder of the projection period.

Chart 15—Estimated Unemployment Fund Cashflow Using Expected Economic Conditions 2009-2018

(In billions of nominal dollars)



Source: Department of Labor

Table 10 shows present values of 10-year projections of revenues and expenditures for the Unemployment Insurance Program using a discount rate of 4.86 percent, the average of the interest rates underlying the 10-year projections. Three sets of numbers are presented in order to show the effects of varying economic conditions as reflected in different assumptions about the unemployment rate. For expected economic conditions, the estimates are based on an unemployment rate of 5.58 percent during fiscal year 2009, decreasing to 4.80 percent in fiscal year 2013 and thereafter. Under the mild recession scenario, the unemployment rate peaks at 7.43 percent in fiscal year 2011 and declines gradually until reaching 4.80 percent in 2017. Finally, under the deep recession scenario, the unemployment rate is assumed to peak at 10.14 percent in 2012 and gradually fall to 5.25 percent by the end of the projection period.

Each scenario uses an open group that includes current and future participants of the Unemployment Insurance Program. Table 10 shows that, as economic conditions worsen, while tax income is projected to increase as higher layoffs result in higher employer taxes, benefit outlays increase much faster. From the Governmentwide (budget) perspective, under expected conditions, the present value of income exceeds the present value of expenditures by $13.7 billion. From the same perspective, under a deep recession scenario, the present value of expenditures exceeds the present value of income by $69.2 billion. From a trust fund perspective, the program has $72 billion in assets. When combined with the present value of net cash income under expected economic conditions, the program has a surplus of $85.8 billion.

Table 10
Present Values of 10-Year Projections of Revenues and Expenditures for Unemployment Insurance Under Three Alternative Scenarios for Economic Conditions

(In billions of present value dollars, as of September 30, 2008)

	Economic Conditions		
	Expected	Mild Recession	Deep Recession
Future cash income	410.0	461.3	524.9
Future expenditures	396.3	467.9	594.1
Net obligations from budget perspective (expenditures less income)	(13.7)	6.6	69.2
Trust fund assets	72.1	72.1	72.1
Net obligations from trust fund perspective[1]	(85.8)	(65.5)	(2.9)

[1]Net obligations from the trust fund perspective equals net obligations from the budget perspective minus trust fund assets. The negative values in this line are indicative of surpluses.

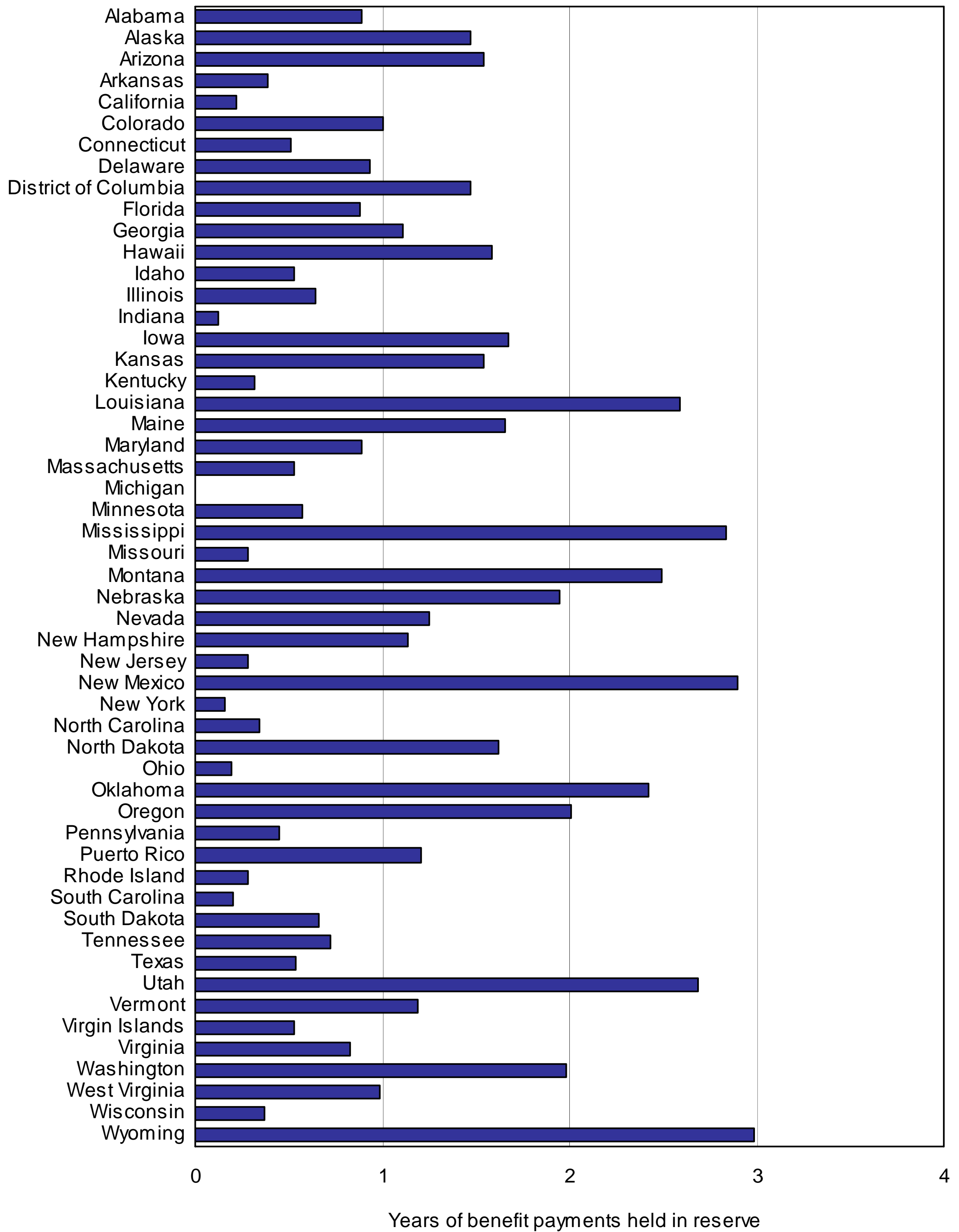
Source: Data for the present value calculations are from the Department of Labor.

Unemployment Trust Fund Solvency

Each State's accumulated UTF net assets or reserve balance should provide a defined level of benefit payments over a defined period. To be minimally solvent, a State's reserve balance should provide for 1 year's projected benefit payment needs based on the highest levels of benefit payments experienced by the State over the last 20 years. A ratio of 1.0 or greater prior to a recession indicates a State is minimally solvent. States below this level are vulnerable to exhausting their funds in a recession. States exhausting their reserve balance must borrow funds from the Federal Unemployment Account (FUA) to make benefit payments. During periods of high-sustained unemployment, balances in the FUA may be depleted. In these circumstances, FUA is authorized to borrow from the Treasury General Fund.

Chart 16 presents the State by State results of this analysis as of September 30, 2008. As the chart illustrates, 29 State funds were below the minimal solvency ratio on September 30, 2008.

Chart 16—Unemployment Trust Fund Solvency as of September 30, 2008



Deferred Maintenance

Deferred maintenance is the estimated cost to bring Government-owned property to an acceptable condition, resulting from not performing maintenance on a timely basis. Deferred maintenance excludes the cost of expanding the capacity of assets or upgrading them to serve needs different from those originally intended. The consequences of not performing regular maintenance could include increased safety hazards, poor service to the public, higher costs in the future, and inefficient operations. Estimated deferred maintenance costs are not accrued in the Statements of Net Cost or recognized as a liability on the balance sheets.

The amounts disclosed for deferred maintenance are allowed to be measured using the following three methods:

- Condition assessment surveys are periodic inspections of the Government-owned property to determine the current condition and estimated cost to bring the property to an acceptable condition.
- Life-cycle cost forecast is an acquisition or procurement technique that considers operation, maintenance, and other costs in addition to the acquisition cost of assets.
- Management analysis method is founded on inflation-adjusted reductions in maintenance funding since the base year.

The amounts disclosed in the table below have all been measured using the condition assessment survey method. The standards for acceptable operating condition and the changes in these standards and changes in asset condition vary widely between the Federal entities.

Some deferred maintenance has been deemed critical. Such amounts and conditions are defined by the individual agencies with responsibility for the safekeeping of these assets. Low and high estimates are based on the materiality of the estimated cost of returning the asset to the acceptable condition versus the total value of the corresponding asset.

Deferred Maintenance as of September 30

	Deferred Maintenance Cost Range					
	Low Estimate		High Estimate		Critical Maintenance	
(In billions of dollars)	2008	2007	2008	2007	2008	2007
Asset category:						
Buildings, structures and facilities	88.6	89.9	94.1	97.2	5.0	12.5
Furniture, fixtures and equipment	0.3	0.2	0.3	0.3	0.1	0.2
Other general property, plant, and equipment	11.9	6.4	12.0	6.4	0.2	0.2
Heritage assets	7.0	3.9	7.0	5.3	-	0.2
Stewardship land	2.2	-	3.2	-	-	-
Total deferred maintenance	110.0	100.4	116.6	109.2	5.3	13.1

Please refer to the individual financial statements of DOD, USDA, DOE, VA, DOI, and NASA for detailed significant information on deferred maintenance, including the standards used for acceptable operating condition and changes in asset condition. These agencies comprise 81 percent of the Government's total reported net property, plant, and equipment of $737.7 billion as of September 30, 2008.

Unexpended Budget Balances

The Federal budget and budget process largely use obligational accounting – a distinct administrative control through which Federal Agencies control, monitor, and report on the status of funds at their disposal. Unexpended budget balances consist of the unobligated and obligated, but unliquidated, budget balances.

Unobligated budget balances, including amounts for trust funds, are the cumulative amount of budget balances that are not obligated and that remain available for obligation. In 1-year accounts, the unobligated balance is not available for new obligations after the end of the fiscal year. In multiyear accounts, the unobligated balance may be carried forward and remains available for obligation for the period specified. In no-year accounts, the unobligated balance is carried forward until specifically rescinded by law or until the purposes for which it was provided have been accomplished. The total unobligated budget balances as of September 30, 2007, and 2006 are $471.1 billion and $463.3 billion, respectively.

Obligated budget balances are the cumulative budget balances that have been obligated but not liquidated. The obligated balance can be carried forward for a maximum of 5 years after the appropriation has expired. The total obligated budget balances as of September 30, 2007 and 2006 are $1,078.3 billion and $977.6 billion, respectively.

The President's Budget with fiscal year 2008 actuals is expected to be published in February 2009. The President's Budget is located at www.whitehouse.gov/omb; unexpended budget balances are shown in the supporting documentation section under "Balances of Budget Authority." The President's fiscal year 2009 Budget (issued on February 4, 2008), includes the estimates of the unobligated and obligated amounts for fiscal year 2008. However, these estimated amounts are expected to differ from the actual amount and are therefore not reported.

Tax Burden

The Internal Revenue Code provides for progressive tax rates, whereby higher incomes are generally subject to higher tax rates. The following tables present the latest available information on income tax and related income, deductions, and credit for individuals by income level and for corporations by size of assets.

Individual Income Tax Liability for Tax Year 2006

Adjusted Gross Income (AGI)	Number of Taxable Returns (In thousands)	AGI (In millions of dollars)	Total Income Tax (In millions of dollars)	Average AGI per Return (In whole dollars)	Average Income Tax per Return (In whole dollars)	Income Tax as a Percentage of AGI
Under $15,000	37,614	188,624	3,141	5,015	84	1.7%
$15,000 under $30,000	29,649	655,386	22,562	22,105	761	3.4%
$30,000 under $50,000	24,907	973,569	59,846	39,088	2,403	6.1%
$50,000 under $100,000	30,053	2,123,894	185,019	70,672	6,156	8.7%
$100,000 under $200,000	12,110	1,610,028	210,538	132,956	17,386	13.1%
$200,000 or more	4,088	2,431,160	545,226	594,740	133,380	22.4%
Total	138,421	7,982,661	1,026,332			

Corporation Income Tax Liability for Tax Year 2005

Total Assets (In thousands of dollars)	Income Subject to Tax (In millions of dollars)	Total Income Tax after Credits (In millions of dollars)	Percentage of Income Tax after Credits to Taxable Income
Zero assets	19,086	5,094	26.7%
$1 under $500	9,223	1,698	18.4%
$500 under $1,000	4,473	1,043	23.3%
$1,000 under $5,000	14,935	4,372	29.3%
$5,000 under $10,000	9,367	3,060	32.7%
$10,000 under $25,000	13,506	4,456	33.0%
$25,000 under $50,000	13,459	4,366	32.4%
$50,000 under $100,000	14,239	4,624	32.5%
$100,000 under $250,000	31,250	9,935	31.8%
$250,000 or more	1,071,781	273,431	25.5%
Total	1,201,319	312,079	

Tax Gap

The tax gap is the aggregate amount of tax (i.e., excluding interest and penalties) that is imposed by the tax laws for any given tax year but is not paid voluntarily and timely. The Internal Revenue Service (IRS) currently projects that the annual Federal gross tax gap is estimated at $345.0 billion. This estimate is based on the results of the National Research Program (NRP). The NRP was a study conducted to measure the compliance rate of the individual filers based on examination of a statistical sample of their filed returns for tax year 2001. The tax gap arises from three types of noncompliance: not filing timely tax returns (the nonfiling gap), underreporting the correct amount of tax on timely-filed returns (the underreporting gap), and not paying on time the full amount reported on timely-filed returns (the underpayment gap). Of these three components, only the underpayment gap is observed; the nonfiling gap and the underreporting gap must be estimated. Each instance of noncompliance by a taxpayer contributes to the tax gap, whether the IRS detects it, and whether the taxpayer is even aware of the noncompliance. The tax gap does not include underpayments by corporate taxpayers or include taxes that should have been paid on income from the illegal sector of the economy.

Underreporting of income tax, employment taxes, and other taxes represents 83 percent of the tax gap. The single largest subcomponent of underreporting involves individuals understating their income, taking improper deductions, overstating business expenses, and erroneously claiming credits. Individual underreporting represents about half of the total tax gap. Individual income tax also accounts for about half of all tax liabilities.

The collection gap is the cumulative amount of assessed tax, penalties, and interest that the IRS expects to remain uncollectible. In essence, it represents the difference between the total balance of unpaid assessments and the net taxes receivable reported on the IRS' balance sheet. The tax gap and the collection gap are related and overlapping concepts, but they have significant differences. The collection gap is a cumulative balance sheet concept for a particular point in time, while the tax gap is like an income statement item for a single year. Moreover, the tax gap estimates include all noncompliance, while the collection gap includes only amounts that have been assessed (a small portion of all noncompliance).

Other Claims for Refunds

Management has estimated amounts that may be paid out as other claims for tax refunds. This estimate represents an amount (principal and interest) that may be paid for claims pending judicial review by the Federal courts or, internally, by appeals. The total estimated payout (including principal and interest) for claims pending judicial review by the Federal courts is $5.0 billion and $8.8 billion for fiscal years 2008 and 2007, respectively. For those under appeal, the estimated payout is $17.0 billion and $5.9 billion for fiscal years 2008 and 2007, respectively. There are also unasserted claims for refunds of certain excise taxes. Although these refund claims have been deemed to be probable, they do not meet the criteria in SFFAS No. 5 for reporting the amounts in the balance sheets or for disclosure in the Notes to the Financial Statements. However, they meet the criteria in SFFAS No. 7 for inclusion as supplemental information. To the extent judgments against the Government for these claims prompt other similarly situated taxpayers to file similar refund claims, these amounts could become significantly greater.

Tax Assessments

The Government is authorized and required to make inquiries, determinations, and assessments of all taxes which have not been duly paid. Unpaid assessments result from taxpayers filing returns without sufficient payment, as well as enforcement programs such as examination, under-reporter, substitute for return and combined annual wage reporting. Assessments with little or no future collection potential are called write-offs. Although compliance assessments and write-offs are not considered receivables under Federal accounting standards, they represent legally enforceable claims of the Government. There is, however, a significant difference in the collection potential between compliance assessments and receivables.

Management's best estimate of additional revenues that may potentially be collected by agencies from compliance assessments and pre-assessment work in process are $69.1 billion and $67.7 billion for fiscal years 2008 and 2007, respectively. The amount of assessments that agencies have statutory authority to collect at the end of the period, but have been written off and excluded from accounts receivable are $99.3 billion and $100.2 billion for fiscal years 2008 and 2007, respectively.

Risk Assumed

Risk assumed information is important for all Federal insurance and guarantee programs, except those relating to social insurance, life insurance and loan guarantee programs. Risk assumed is generally measured by the present value of unpaid expected losses net of associated premiums based on the risk inherent in the insurance or guarantee coverage in force. In addition to the liability for unpaid insurance claims included in Note 15─Insurance Program Liabilities, for events that have already occurred, the Government is also required to report as supplementary information risk assumed amounts and the periodic changes in those amounts.

The assessments of losses expected based on the risk assumed are based on actuarial or financial methods applicable to the economic, legal and policy environment in force at the time the assessments are made. Management has estimated the loss amounts based on the risk assumed as well as the periodic changes.

Please refer to the individual financial statements of the Pension Benefit Guaranty Corporation, the Department of Agriculture, and the Department of Veterans Affairs for other significant detailed information.

Risk Assumed Information as of September 30

(In billions of dollars)	2008	2007
Present Value of unpaid expected losses, net of associated premiums:		
Pension Benefit Guaranty Corporation	46.8	65.7
Department of Agriculture	9.9	6.6
Department of Veterans Affairs	0.8	-
All other	0.6	0.7
Total	58.1	73.0
Periodic changes in risk assumed amounts:		
Pension Benefit Guaranty Corporation	(19.0)	(7.6)
Department of Agriculture	3.3	2.1
Total	(15.7)	(5.5)

Treasury did not record a contingent liability for any risk assumed related to the temporary guarantee program for money market funds because Treasury's exposure under the program is the difference between a stable share price and the net asset value at liquidation of the money market fund. For all of the reasons outlined in Note 8 and based on current information and the Federal programs in place, and as this is a temporary program dealing with issues of first impression, the risk of loss to the Government is believed to be negligible.

The liquidity commitment to the GSE described in the senior preferred stock purchase agreements section of Note 8 is essentially an insurance program in that the Treasury received a commitment fee in return for a guarantee of GSE liquidity should their liabilities exceed their assets at the end of any future quarter. The total program liability as of September 30, 2008, should include the amount of quarterly liquidity draws requested but not yet paid, accruals for amounts of liquidity draws not known until after the end of the quarter, and an estimated contingent liability for the discounted present value of future liquidity draws up to the $200 billion combined liability limit. The discounted present value would take into account estimated offsetting increases in the liquidity preference of the preferred stock, increases in dividends on the increased liquidity preference, and annual commitment fees. However, due to the current uncertainties and turbulence in the financial markets, for fiscal year 2008 the estimated contingent liability amount does not have "sufficient reliability" to be recorded as a liability. The only liability that is recorded for this activity for fiscal year 2008 is the $13.8 billion draw request received from the Federal Housing Financing Agency on behalf of Freddie Mac in November 2008 for the quarter ended September 30, 2008. As noted above, the total gross risk under this commitment was $200 billion; after the November draw request, the remaining commitment is $186.2 billion.

Unmatched Transactions and Balances

(In millions of dollars)	Fiscal Year 2008	Fiscal Year 2007
Change in intra-Governmental unmatched balances:		
Debt/investment	343.0	2,137.0
Interest payable/receivable	(35.1)	(73.6)
Loans payable/receivable	1,843.1	5,602.4
Benefit program contributions payable/receivable	(514.9)	53.3
Accounts payable/receivable	2,502.1	(2,093.7)
Advances from/to others and deferred credits/prepayments	3,877.2	(209.1)
Transfers payable/receivable	9.0	(523.3)
	8,024.4	4,893.0
Unmatched intra-Governmental transactions:		
Federal securities interest revenue/expense - investment exchange	570.2	(830.0)
Borrowings interest revenue/expense - exchange	1,532.4	(1,058.1)
Borrowings gains/losses	(54.7)	(6.8)
Nonexpenditure transfers-in/out	1,352.2	6,600.1
Expenditure transfers-in/out	5,279.5	(855.8)
Transfers-in/out without reimbursement	(2,974.0)	5,508.6
Imputed financing source/cost	(13.1)	(8.9)
Benefit program revenue/cost	1,551.8	1,961.7
	7,244.3	11,310.8
General fund transactions:		
Fund balance with Treasury	(38,370.7)	(18,149.1)
Appropriations of unavailable special or trust fund receipts - transfers out	1,032.1	2,781.4
Appropriations of unavailable special or trust fund receipts - transfers in	744.0	(1,585.4)
Appropriations received/warrants	(31,000.7)	(133,251.2)
Other general fund transactions	82,826.6	120,149.7
	15,231.3	(30,054.6)
Net intra-agency reporting errors	(751.9)	7,171.3
Unmatched transactions and balances, net	29,748.1	(6,679.5)

( ) Parentheses indicate a decrease to Net Position.

The Statement of Operations and Changes in Net Position includes an amount for unmatched transactions and balances that result from the consolidation of Federal reporting entities. Transactions between Federal entities must be eliminated in consolidation to calculate the financial position of the U.S. Government. Many of the amounts included in the table represent intragovernmental activity and balances that differed between Federal agency trading partners and often totaled significantly more in the absolute than the net amounts shown. In addition, included in the "General Fund Transactions" section are certain intragovernmental accounts, primarily related to agency unreconciled transactions with the General Fund, totaling hundreds of billions of dollars. The table also reflects other consolidating adjustments and other adjustments that contributed to the unmatched transactions and balances amount.

Unmatched transactions and balances between Federal entities impact not only in the period in which differences originate but also in the periods where differences are reconciled. As a result, it would not be proper to conclude that increases or decreases in the unmatched amounts shown in the "Unmatched Transactions and Balances" table reflect improvements or deteriorations in the Government's ability to reconcile intragovernmental transactions. The Federal community considers the identification and accurate reporting of intragovernmental activity a priority.

United States Government Stewardship Information (Unaudited) for the Years Ended September 30, 2008, and September 30, 2007

Stewardship Investments

Stewardship investments focus on Government programs aimed at providing long-term benefits by improving the Nation's productivity and enhancing economic growth. These investments can be provided through direct Federal spending or grants to State and local governments for certain education and training programs, research and development, and federally financed but not federally-owned property, such as bridges and roads. When incurred, these investments are included as expenses in determining the net cost of operations. Stewardship investments for the current year and for the immediately preceding 4 years are shown below in Table 11. The amounts reported in fiscal year 2008 for investments in prior years (fiscal years 2007-2004) are restated due to agencies continuously reviewing, correcting, and updating this data.

Table 11
Stewardship Investments
for the Years Ended September 30

(In billions of dollars)	Fiscal Year 2008	Restated Fiscal Year 2007	Restated Fiscal Year 2006	Restated Fiscal Year 2005	Restated Fiscal Year 2004
Investments in non-Federal physical property	57.8	56.2	54.4	51.9	54.8
Investments in human capital	77.2	76.1	107.4	88.2	76.6
Research and development:					
Investments in basic research	27.6	26.5	25.2	25.1	23.4
Investments in applied research	21.4	22.2	21.7	21.2	20.0
Investments in development	79.2	66.3	52.1	42.1	37.9
Total investments	263.2	247.3	260.8	228.5	212.7

Non-Federal Physical Property

The Government makes grants and provides funds for the purchase, construction, and/or major renovation of State and local government physical properties. Cost for non-Federal physical property programs are included as expenses in the Statements of Net Cost and are reported as investments in Table 11. They are measured on the same accrual basis of accounting used in the *Financial Report* statements.

The DOT, the HUD, and the Environmental Protection Agency (EPA) had $48.9 billion (85 percent), $3.7 billion (6 percent), and $2.7 billion (5 percent), respectively, of the total non-Federal physical property investments in fiscal year 2008 as shown in Table 11. These same agencies also had similar investment amounts (and percentage contributions) in each of the preceding 4 years.

Within DOT, the Federal Highway Administration invested $35.3 billion during fiscal year 2008, primarily via reimbursement from the Highway Trust Fund, of States' construction costs related to interstate and national highways. The States' contribution is 10 percent for the Interstate System and 20 percent for most other programs. These highway programs have not typically resulted in significant transfers of property to State or local governments.

The significant programs administered by HUD relate to grants for property renovation and public housing programs. The significant programs administered by the EPA relate to grants for the nation's drinking water and clean water infrastructure. Neither of these programs typically transfers property to State or local governments.

Human Capital

The Government runs several programs that invest in human capital. Those investments go toward increasing and maintaining a healthy economy by educating and training the general public. Costs do not include training expenses for Federal workers.

The Department of Education (Education), the Department of Labor (DOL), and the Department of Veterans Affairs (VA) had $62.8 billion (81 percent), $5.8 billion (8 percent), and $3.6 billion (5 percent), respectively, of the total human capital investments in fiscal year 2008 as shown in Table 11. These same agencies also had similar investment amounts (and percentage contributions) in each of the preceding 4 years, with the exception of Education in fiscal year 2007, where there was a decrease in Federal Family Education Loan and Direct Loan subsidy re-estimates and subsidy transfers due to decreased loan consolidation activity during the current and prior year.

Education administers a wide variety of programs related to general public education and training programs that are intended to increase or maintain national economic productive capacity. Within Education, approximately 32 percent of the annual investment in fiscal year 2008 relates to Federal student aid, either in the form of direct or guaranteed loans or grants to eligible undergraduate and graduate students. The remaining investments primarily relate to grants for Elementary, Secondary, and Special Education programs as well as for various departmental initiatives (e.g., charter schools, foreign language assistance, etc.).

The significant human capital programs administered by DOL relate to grants for job training and employment programs. The significant human capital programs administered by VA also relate to grants for job training and rehabilitation programs for veterans.

Research and Development

Federal investments in research and development (R&D) comprise those expenses for basic research, applied research, and development that are intended to increase or maintain national economic productive capacity or yield other future benefits.

- Investments in basic research are for systematic studies to gain knowledge or understanding of the fundamental aspects of phenomena and of observable facts without specific applications toward processes or products in mind.
- Investments in applied research are for systematic studies to gain knowledge or understanding necessary for determining the means by which a recognized and specific need may be met.
- Investments in development are the systematic use of the knowledge and understanding gained from research for the production of useful materials, devices, systems, or methods, including the design and development of prototypes and processes.

With regard to basic and applied research, the Department of Health and Human Services (HHS) had $16.6 billion (60 percent) and $11.4 billion (53 percent), of the total basic and applied research investments, respectively, in fiscal year 2008 as shown in Table 11. HHS also had similar R&D investment amounts (and percentage contributions) in each of the preceding 4 years.

Within HHS, the National Institutes of Health (NIH) conducts almost all (97 percent) of the department's basic and applied research. The NIH Research Program includes all aspects of the medical research continuum, including basic and disease-oriented research, observational and population-based research, behavioral research, and clinical research, including research to understand both health and disease states, to move laboratory findings into medical applications, to assess new treatments or compare different treatment approaches; and health services research.

The NIH regards the expeditious transfer of the results of its medical research for further development and commercialization of products of immediate benefit to improved health as an important mandate.

With regard to development, the DOD and the NASA had $65.2 billion (82 percent) and $11.4 billion (14 percent), respectively, of total development investments in fiscal year 2008, as shown in Table 11. DOD changed its methodology for reporting yearly investments in research and development during fiscal year 2008 which affected the current and prior 4 years. Their data is based on research and development outlays (expenditures). As a result, the total amounts of investments in development (Table 11) have been restated. Development is comprised of five stages: advanced technology development, advanced component development and prototypes, system development and demonstration, management support, and operational systems development. Major outcomes of DOD development are:

- Hardware and software components, or complete weapon systems, ready for operational and developmental testing and field use, and
- Weapon systems finalized for complete operational and developmental testing.

NASA development programs include activities to extend our knowledge of Earth, its space environment, and the universe, and to invest in new aeronautics and advanced space transportation technologies that support the development and application of technologies critical to the economic, scientific, and technical competiveness of the United States. Some outcomes and future outcomes of this development are:

- The Constellation Systems program to develop, demonstrate, and deploy the capabilities to transport crew and cargo for missions to the lunar surface and safely return the crew to Earth.
- Robotic spacecraft that use electrical power for propulsion, data acquisition, and communication to accurately place themselves in orbit around the surfaces of bodies about which we may know relatively little.
- The Fundamental Aeronautics Program conducts research to enable the design of vehicles that fly through any atmosphere at any speed. A key focus will be the development of physics-based, multidisciplinary design, analysis, and optimization tools to address the multiple design challenges in future aircraft.
- The James Webb Space Telescope is a large, deployable infrared astronomical space-based observatory. The mission is a logical successor to the Hubble Space Telescope, extending beyond Hubble's discoveries into the infrared, where the highly red shifted early universe must be observed, where cool objects like protostars and protoplanetary disks emit strongly, and where dust obscures shorter wavelengths.
- The study of the dynamic Earth system to trace effect to cause, connect variability and forcing with response, and vastly improve national capabilities to predict climate, weather, natural hazards, and conditions in the space environment.

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Appendix: Significant Government Entities

This appendix list the organizations and agencies encompassed in the reporting entity for this publication. The reporting entity is a specifically defined group of agencies, principally cabinet departments and other agencies of the executive branch, as stated in the law and accounting guidance.

The determination as to which organizations and agencies will be included in the reporting entity is governed by Federal laws and is also based on guidance issued by the Federal Accounting Standards Advisory Board in their Statement of Federal Financial Accounting Concept No. 2, Entity and Display, which provides criteria for determining what should be included in the reporting entity for a consolidated Governmentwide report. The Board is now considering more specific guidance on the reporting entity for this report.

There are a total of 147 organizations and agencies included in the Financial Report of the United States Government. The lists below describe three groups of entity types that comprise the reporting entity for the *Financial Report*.

Twenty-Four Chief Financial Officer Act Agencies

Department of Agriculture
www.usda.gov
Department of Commerce
www.doc.gov
Department of Defense
www.defenselink.mil
Department of Education
www.ed.gov
Department of Energy
www.doe.gov
Department of Health and Human Services
www.hhs.gov
Department of Homeland Security
www.dhs.gov
Department of Housing and Urban Development
www.hud.gov
Department of the Interior
www.doi.gov
Department of Justice
www.usdoj.gov
Department of Labor
www.dol.gov
Department of State
www.state.gov
Department of Transportation
www.dot.gov
Department of the Treasury
www.ustreas.gov
Department of Veterans Affairs
www.va.gov
Environmental Protection Agency
www.epa.gov
General Services Administration
www.gsa.gov
National Aeronautics and Space Administration
www.nasa.gov
National Science Foundation
www.nsf.gov
Office of Personnel Management
www.opm.gov
Small Business Administration
www.sba.gov
Social Security Administration
www.ssa.gov
U.S. Agency for International Development
www.usaid.gov
U.S. Nuclear Regulatory Commission
www.nrc.gov

Eleven Additional Significant Entities

Export-Import Bank of the United States
www.exim.gov
Farm Credit System Insurance Corporation
www.fcsic.gov
Federal Communications Commission
www.fcc.gov
Federal Deposit Insurance Corporation
www.fdic.gov
National Credit Union Administration
www.ncua.gov
Pension Benefit Guaranty Corporation
www.pbgc.gov
Railroad Retirement Board
www.rrb.gov
Securities and Exchange Commission
www.sec.gov
Smithsonian Institution
www.si.edu
Tennessee Valley Authority
www.tva.gov
U.S. Postal Service
www.usps.gov

One Hundred Twelve Additional Entities

Abraham Lincoln Bicentennial Commission
Advisory Council on Historic Preservation
African Development Fund
American Battle Monuments Commission
America's Education Goals Panel
Antitrust Modernization Commission
Appalachian Regional Commission
Appalachian Regional Development Fund
Architect of the Capitol
Architectural and Transportation Barriers Compliance Board
Armed Forces Retirement Home
Barry Goldwater Scholarship and Excellence in Education Foundation
Broadcasting Board of Governors
Central Intelligence Agency
Chemical Safety Hazard Investigation Board
Christopher Columbus Fellowship Foundation
Commission for the Preservation of America's Heritage Abroad
Commission of Fine Arts
Commission on Affordable Housing and Health Facility Needs for Seniors in the 21st Century
Commission on Civil Rights
Commission on International Religious Freedom
Commission on Ocean Policy
Commission on Online Child Protection
Commission on Review of Overseas Military Facility Structure United States
Commission on Security and Cooperation–Europe
Commission on Weapons of Mass Destruction
Committee for Purchase from People who are Blind or Severely Disabled
Commodity Futures Trading Commission
Community Management Staff
Congressional Budget Office
Congressional-Executive Commission on the People's Republic of China
Consumer Product Safety Commission
Corporation for National and Community Service
Court of Appeals for Veterans Claims
Court Services and Offender Supervision Agency for DC
DC Courts
DC Courts–Defender Services
Defense Nuclear Facilities Safety Board
Delta Regional Authority
Denali Commission
Dwight D. Eisenhower Memorial Commission
Eisenhower Exchange Fellowship Program
Election Assistance Commission
Environmental Dispute Resolution Fund
Equal Employment Opportunity Commission
Executive Office of the President
Farm Credit Administration
Federal Election Commission
Federal Financial Institutions Examination Council Appraisal Subcommittee
Federal Housing Finance Agency
Federal Housing Finance Board
Federal Labor Relations Authority
Federal Maritime Commission
Federal Mediation and Conciliation Service
Federal Mine Safety and Health Review Commission
Federal Trade Commission
Government Accountability Office
Government Printing Office
Harry S. Truman Scholarship Trust Fund
Institute of Museum Services
Interagency Council on the Homeless
Inter-American Foundation
International Trade Commission
James Madison Memorial Fellowship Foundation
Japan-United States Friendship Commission
John C. Stennis Center
John F. Kennedy Center for the Performing Arts

Library of Congress
Marine Mammal Commission
Medicare Payment Advisory Commission
Merit Systems Protection Board
Military Sales Program
Millennium Challenge Corporation
Morris K. Udall Scholarship Foundation
National Archives and Records Administration
National Capital Planning Commission
National Commission on Libraries and Information Science
National Commission on Terrorist Attacks upon the United States
National Council on Disability
National Endowment for the Arts
National Endowment for the Humanities
National Gallery of Art
National Labor Relations Board
National Mediation Board
National Railroad Retirement Investment Trust
National Veterans Business Development Corporation
Neighborhood Reinvestment Corporation
Nuclear Waste Technical Review Board
Occupational Safety and Health Review Commission
Office of Compliance
Office of Government Ethics
Office of Navajo and Hopi Indian Relocation
Office of Special Counsel
Office of the Federal Coordination for Alaska Natural Gas Transportation Projects
Open World Leadership Center Funds
Overseas Private Investment Corporation
Panama Canal Commission
Peace Corps
Presidio Trust
Public Defender Service
Selective Service System
Senate Preservation Fund
St. Lawrence Seaway Development Corporation
State Justice Institute
U.S. Capital Preservation Commission
U.S. China Security Review Commission
U.S. Holocaust Memorial Museum
U.S. Institute of Peace
U.S. Trade and Development Agency
Vietnam Education Foundation
White House Commission on the National Moment of Remembrance
Woodrow Wilson International Center for Scholars

Legislative and Judicial Branches

There are no legal or other requirements for the legislative or judicial branch to prepare audited financial statements or to provide accrual-based accounting data for inclusion in the Governmentwide financial statements. Therefore, these consolidated statements do not include accrual-based accounting data for such entities as the U.S. Courts or the Congress. Some legislative branch entities voluntarily prepare and submit such information (e.g., Government Accountability Office, Government Printing Office, and Library of Congress). The President's Budget includes cash-based, outlay data for the legislative and judicial branches and, to a limited extent, this outlay data is also a part of the information contained in this report.

Entities Excluded from these Statements

The following entities are not part of the Governmentwide reporting entity based on an assessment of these entities in accordance with the indicative criteria stated in SFFAC No. 2, Entity and Display. However, this list is not all inclusive of all entities excluded from these statements.

Board of Governors of the Federal Reserve System (Including the Federal Reserve Banks)
Federal Home Loan Banks
Federal Home Loan Mortgage Corporation (Freddie Mac)
Federal National Mortgage Association (Fannie Mae)
Federal Retirement Thrift Investment Board (Including the Thrift Savings Fund)
Financing Corporation
Resolution Funding Corporation
Student Loan Marketing Association (SLMA or Sallie Mae)

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United States Government Accountability Office
Washington, DC 20548

The President
The President of the Senate
The Speaker of the House of Representatives

The Secretary of the Treasury, in coordination with the Director of the Office of Management and Budget, is required annually to submit financial statements for the U.S. government to the President and the Congress. GAO is required to audit these statements.[1] This is (1) our report on the accompanying U.S. government's accrual basis consolidated financial statements for the fiscal years ended September 30, 2008 and 2007, and the 2008, 2007, and 2006 Statements of Social Insurance, and (2) our associated reports on internal control and compliance with significant laws and regulations. As used in this report, accrual basis financial statements refer to all of the consolidated financial statements and notes, except for those related to the Statement of Social Insurance.[2]

The federal government is responsible for (1) preparing annual consolidated financial statements in conformity with U.S. generally accepted accounting principles (GAAP); (2) establishing, maintaining, and assessing internal control to provide reasonable assurance that the control objectives of the Federal Managers' Financial Integrity Act (FMFIA)[3] are met; and (3) complying with significant laws and regulations. Also, the 24 Chief Financial Officers (CFO) Act agencies are responsible for implementing and maintaining financial management systems that substantially comply with Federal Financial Management Improvement Act of 1996 (FFMIA)[4] requirements. Our objective was to

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[1]The Government Management Reform Act of 1994 has required such reporting, covering the executive branch of government, beginning with financial statements prepared for fiscal year 1997. 31 U.S.C. 331(e). The federal government has elected to include certain financial information on the legislative and judicial branches in the consolidated financial statements as well.
[2]The accrual basis consolidated financial statements for the fiscal years ended September 30, 2008 and 2007 consist of the (1) Statements of Net Cost, (2) Statements of Operations and Changes in Net Position, (3) Reconciliations of Net Operating Cost and Unified Budget Deficit, (4) Statements of Changes in Cash Balance from Unified Budget and Other Activities, and (5) Balance Sheets, including the related notes to these financial statements. Most revenues are recorded on a modified cash basis. The 2008, 2007, and 2006 Statements of Social Insurance, including the related notes, are also included in the consolidated financial statements. The Statements of Social Insurance do not interrelate to the accrual basis consolidated financial statements.
[3]31 U.S.C. 3512 (c), (d) (commonly referred to as FMFIA). This act requires executive agency heads to evaluate and report annually to the President and the Congress on the adequacy of their internal control and accounting systems and on actions to correct significant problems.
[4]31 U.S.C. 3512 note (Federal Financial Management Improvement Act).

audit the consolidated financial statements for the fiscal years ended September 30, 2008 and 2007. Appendix I discusses the scope and methodology of our work.

Material weaknesses[5] discussed later in our report continued to (1) hamper the federal government's ability to reliably report a significant portion of its assets, liabilities, costs, and other related information; (2) affect the federal government's ability to reliably measure the full cost as well as the financial and nonfinancial performance of certain programs and activities; (3) impair the federal government's ability to adequately safeguard significant assets and properly record various transactions; and (4) hinder the federal government from having reliable financial information to operate in an efficient and effective manner. We found the following:

- Certain material weaknesses in financial reporting and other limitations on the scope of our work[6] resulted in conditions that continued to prevent us from expressing an opinion on the accompanying accrual basis consolidated financial statements for the fiscal years ended September 30, 2008 and 2007.[7]

- The Statements of Social Insurance for 2008 and 2007[8] are presented fairly, in all material respects, in conformity with GAAP; we disclaim an opinion on the 2006 Statement of Social Insurance.[9]

- The federal government did not maintain effective internal control over financial reporting (including safeguarding assets) and compliance with significant laws and regulations as of September 30, 2008.

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[5]A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected. A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis.

[6]Three major impediments continue to prevent us from rendering an opinion on the accrual basis consolidated financial statements: (1) serious financial management problems at the Department of Defense, (2) the federal government's inability to adequately account for and reconcile intragovernmental activity and balances between federal agencies, and (3) the federal government's ineffective process for preparing the consolidated financial statements.

[7]We previously reported that certain material weaknesses prevented us from expressing an opinion on the consolidated financial statements of the U.S. government for fiscal years 1997 through 2006 and on the accrual basis consolidated financial statements of the U.S. government for fiscal year 2007.

[8]The valuation date is January 1 for all social insurance programs except the Black Lung program, which valuation date is September 30.

[9]We disclaimed an opinion on the fiscal year 2006 consolidated financial statements, including the Statement of Social Insurance.

- Our work to test compliance with selected provisions of significant laws and regulations in fiscal year 2008 was limited by the material weaknesses and scope limitations discussed in this report.

Significant Matters of Emphasis—The Federal Government's Response to Stabilize Financial Markets and Its Long-Term Fiscal Challenges

Before discussing our disclaimer of opinion on the accrual basis consolidated financial statements for fiscal years 2008 and 2007 and on the 2006 Statement of Social Insurance, and our unqualified opinions on the 2008 and 2007 Statements of Social Insurance, the following key items deserve emphasis in order to put the information contained in the financial statements and the Management's Discussion and Analysis section of the *2008 Financial Report of the United States Government* (*2008 Financial Report*) into context.

The unprecedented actions that the federal government is taking to restore stability to the financial markets will likely have a significant effect on the federal government's financial condition, at least in the short-term, through increased borrowing. In addition, the current recession could significantly affect the federal government's future tax revenues and the value of certain of its assets and liabilities, such as loans and loan guarantees. The ultimate effect of these actions and the recession on the federal government's financial condition are not yet known and will not be fully reflected in the consolidated financial statements and *The Budget of the United States Government* until fiscal year 2009 and beyond. For example, the federal government placed the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) into conservatorship and committed to (1) provide capital of up to $200 billion ($13.8 billion of which was recorded as a liability at September 30, 2008), (2) make short-term loans to the entities, and (3) buy mortgage-backed securities issued by the entities.[10] Also, under the Troubled Asset Relief Program (TARP)[11] established in fiscal year 2009, the federal government may purchase, up to $700 billion,[12] or insure "troubled assets". Substantial purchases have been made thus far under TARP. Further, the federal government borrowed money to increase its cash deposits at the Federal Reserve to support the Federal Reserve's market stabilization actions (as of September 30, 2008, the deposit balance was $300 billion). These and other actions that the federal government has taken to stabilize financial markets and restore the availability of credit for Americans are discussed in the Management Discussion and Analysis section of the *2008 Financial Report* and Notes 2, 4, 8, 20, and 25 of the consolidated financial statements.

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[10]The Housing and Economic Recovery Act of 2008 (Pub. L. No. 110-289) authorizes the Department of the Treasury to purchase, for a limited amount of time, any amount of Fannie Mae or Freddie Mac securities, whether debt or equity.

[11]The TARP was established by the Department of the Treasury under authority provided in the Emergency Economic Stabilization Act of 2008 (Pub. L. No. 110-343). The Act requires the U.S. Comptroller General to report every 60 days on a variety of areas associated with oversight of TARP. For the initial 60-day report see GAO, *Troubled Asset Relief Program*, GAO-09-161 (Washington, D.C.: December 3, 2008).

[12]The $700 billion purchase limit is reduced by an amount equal to the difference between the total of the outstanding insured obligations and the balance in the Troubled Assets Insurance Financing Fund.

Currently, policymakers are understandably focused on dealing with stabilizing financial markets and stimulating the economy. However, once these issues are addressed, the nation's new and returning leaders will need to turn their attention to the serious long-term challenges of addressing the federal government's large and growing structural deficits that are driven primarily by rising health care costs and known demographic trends. As discussed in this *2008 Financial Report*, the federal government is on an unsustainable long-term fiscal path. The federal government faces increasing pressures yet a shrinking window of opportunity for phasing in adjustments.

DISCLAIMER OF OPINION ON THE ACCRUAL BASIS CONSOLIDATED FINANCIAL STATEMENTS

Because of the federal government's inability to demonstrate the reliability of significant portions of the U.S. government's accompanying accrual basis consolidated financial statements for fiscal years 2008 and 2007, principally resulting from certain material weaknesses, and other limitations on the scope of our work, described in this report, we are unable to, and we do not, express an opinion on such accrual basis consolidated financial statements.

As a result of these limitations, readers are cautioned that amounts reported in the accrual basis consolidated financial statements and related notes may not be reliable. These material weaknesses and other scope limitations also affect the reliability of certain information contained in the accompanying Management's Discussion and Analysis and other financial management information—including information used to manage the federal government day to day and budget information reported by federal agencies—that is taken from the same data sources as the accrual basis consolidated financial statements.

We have not audited and do not express an opinion on the Management's Discussion and Analysis, or on Stewardship Information, Supplemental Information, or other information that is not part of the consolidated financial statements and related notes included in the *2008 Financial Report*.

As discussed in Note 21 to the consolidated financial statements, the fiscal year 2007 Balance Sheet and Statement of Operations and Changes in Net Position were both restated to correct certain earmarked activity and balances. Last year, we disclaimed an opinion on the fiscal year 2007 accrual basis consolidated financial statements due to certain material weaknesses and limitations on the scope of our work, including the material weakness related to the preparation of the consolidated financial statements. Given the material weaknesses and scope limitations discussed below, additional restatements may occur in the future.

Limitations on the Scope of Our Work

For fiscal years 2008 and 2007, there were limitations on the scope of our work in addition to the material weaknesses that contributed to our disclaimer of opinion on the accrual basis consolidated financial statements. First, the Department of the Treasury

(Treasury) and the Office of Management and Budget (OMB) depend on representations from certain federal agencies to provide their representations to us regarding the U.S. government's consolidated financial statements. Treasury and OMB were unable to provide us with adequate representations regarding the U.S. government's accrual basis consolidated financial statements primarily because of insufficient representations provided to them by the Department of Defense (DOD) for fiscal years 2008 and 2007. Second, the final *2008 Financial Report* and *2007 Financial Report* were not provided in time for us to complete all of our planned audit procedures related to the compilation of these reports.

Material Weaknesses Contributing to Our Disclaimer of Opinion on the Accrual Basis Consolidated Financial Statements

The federal government did not maintain adequate systems or have sufficient, reliable evidence to support certain material information reported in the accompanying accrual basis consolidated financial statements, as briefly described below. The underlying material weaknesses in internal control, which generally have existed for years, contributed to our disclaimer of opinion on the accrual basis consolidated financial statements. Appendix II describes the material weaknesses in more detail and highlights the primary effects of these material weaknesses on the accompanying accrual basis consolidated financial statements and on the management of federal government operations. The material weaknesses that contributed to our disclaimer of opinion on the accrual basis consolidated financial statements were the federal government's inability to:

- satisfactorily determine that property, plant, and equipment and inventories and related property, primarily held by DOD, were properly reported in the accrual basis consolidated financial statements;

- reasonably estimate or adequately support amounts reported for certain liabilities, such as environmental and disposal liabilities, or determine whether commitments and contingencies were complete and properly reported;

- support significant portions of the total net cost of operations, most notably related to DOD, and adequately reconcile disbursement activity at certain agencies;

- adequately account for and reconcile intragovernmental activity and balances between federal agencies;

- ensure that the federal government's accrual basis consolidated financial statements were (1) consistent with the underlying audited agency financial statements, (2) properly balanced, and (3) in conformity with GAAP; and

- identify and either resolve or explain material differences between certain components of the budget deficit reported in Treasury's records, which are used to prepare the Reconciliation of Net Operating Cost and Unified Budget Deficit and Statement of Changes in Cash Balance from Unified Budget and Other Activities, and

related amounts reported in federal agencies' financial statements and underlying financial information and records.

Due to the material weaknesses and the additional limitations on the scope of our work discussed above, there may also be additional issues that could affect the accrual basis consolidated financial statements that were not identified.

UNQUALIFIED OPINIONS ON THE STATEMENTS OF SOCIAL INSURANCE FOR 2008 AND 2007

In our opinion, the Statements of Social Insurance for 2008 and 2007 present fairly, in all material respects, the financial condition of the federal government's social insurance programs, in conformity with GAAP. We disclaim an opinion on the 2006 Statement of Social Insurance[13] and have not audited and do not express an opinion on the Statements of Social Insurance for 2005 and 2004, and on other information related to such statements that is included in the accompanying *2008 Financial Report*.

As discussed in Note 23 to the consolidated financial statements, the Statement of Social Insurance presents the actuarial present value of the federal government's estimated future revenue to be received from or on behalf of participants and estimated future expenditures to be paid to or on behalf of participants, based on benefit formulas in current law and using a projection period sufficient to illustrate the long-term sustainability of the social insurance programs.[14] In preparing the Statement of Social Insurance, management considers and selects assumptions and data that it believes provide a reasonable basis for the assertions in the statement. However, because of the large number of factors that affect the Statement of Social Insurance and the fact that such assumptions are inherently subject to substantial uncertainty (arising from the likelihood of future changes in general economic, regulatory, and market conditions, as well as other more specific future events, significant uncertainties, and contingencies), there will be differences between the estimates in the Statement of Social Insurance and the actual results, and those differences may be material. The Supplemental Information section of the *2008 Financial Report* includes unaudited information concerning how changes in various assumptions would change the present value of future estimated expenditures in excess of future estimated revenue. As discussed in that section, Medicare projections are very sensitive to changes in the health care cost growth assumption.

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[13]Beginning in fiscal year 2006, the Statement of Social Insurance became a principal financial statement and was audited as part of the applicable federal agencies' financial statements. We disclaimed an opinion on the fiscal year 2006 consolidated financial statements, including the Statement of Social Insurance. For fiscal years 2008 and 2007, we designed our audit to provide an opinion on the 2008 and 2007 consolidated Statements of Social Insurance, respectively.

[14]The projection period used for the Social Security, Medicare, and Railroad Retirement social insurance programs is 75 years. For the Black Lung program, the projections are through 2040, when the program is scheduled to terminate.

In addition to the inherent uncertainty that underlies the expenditure projections prepared for all parts of Medicare, the Supplementary Medical Insurance (SMI) Part D projections have an added uncertainty in that they were prepared using very little program experience upon which to base the estimates, and the SMI Part B projections assume significant reductions in physician payments, as required under current law, which may or may not occur. The Congress has overridden scheduled reductions in physician payments calculated for each of the last 6 years, including for 2008, and also for 2009.[15] On December 29, 2007, legislation was enacted to override scheduled reductions in payments for the first half of 2008. On July 15, 2008, the Medicare Improvements for Patients and Providers Act (MIPPA) of 2008 was enacted. Many provisions in the MIPPA affected the Medicare program including payments to providers such as physicians and managed care plans, and beneficiary improvements, such as expanded access to care, enrollment assistance, and increased coverage. It is not possible to anticipate what other actions the Congress might take, either in the near or long-term, to alter the scheduled reductions in physician payments. If scheduled reductions continue to be overridden in the future, actual SMI Part B expenditures could be materially greater than the amounts presented in the 2008 Statement of Social Insurance.

The scheduled future benefits reported in the Statement of Social Insurance are based on benefit formulas in current law. However, consistent with the respective annual Trustees Reports, the Social Security and Medicare programs are not sustainable under current financing arrangements. Also, the law concerning these programs can be changed at any time by the Congress. In fact, payment of Social Security and Medicare Hospital Insurance (Part A) benefits are limited by law to the balances in the respective trust funds. Consequently, future scheduled benefits are limited to future revenues plus existing trust fund assets. As discussed in the Supplemental Information section of the *2008 Financial Report*, the Social Security and Medicare Part A trust funds are projected to be exhausted in 2041 and 2019, respectively, at which time they will be unable to pay the full amount of scheduled future benefits. For Social Security, projected future revenues would be sufficient to pay 78 percent of scheduled benefits in 2041, the year of trust fund exhaustion, and decreasing to 75 percent of scheduled benefits in 2082. Similarly, for Medicare Part A, projected future revenues would be sufficient to pay 78 percent of scheduled benefits in 2019, the year of trust fund exhaustion, and decreasing to 30 percent of scheduled benefits in 2082.

Management's Discussion and Analysis, Supplemental Information, and other information included in the accompanying *2008 Financial Report* contain information directly related to the Statements of Social Insurance. We did not audit and do not express an opinion on this information. However, we compared the information that directly related to the Statements of Social Insurance for consistency with the Statements of Social Insurance and discussed the methods of measurement and presentation of such

[15]The Medicare, Medicaid, and SCHIP Extension Act of 2007, Pub. L. No. 110-173, § 101(a)(1)(B), overrode the scheduled reductions for the first six months of calendar year 2008 and the Medicare Improvement for Patients and Providers Act of 2008, Pub. L. No. 110-275, § 131 (a)(1), overrode the scheduled reductions for the last six months of calendar year 2008 and all of 2009.

information with Treasury officials. Based on this limited work, we found no material inconsistencies with the Statements of Social Insurance or GAAP.

ADVERSE OPINION ON INTERNAL CONTROL

Because of the effects of the material weaknesses discussed in this report, in our opinion, the federal government did not maintain effective internal control as of September 30, 2008, to meet the following objectives: (1) transactions are properly recorded, processed, and summarized to permit the preparation of the financial statements and stewardship information in conformity with GAAP, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition; and (2) transactions are executed in accordance with laws governing the use of budget authority and with other significant laws and regulations that could have a direct and material effect on the financial statements and stewardship information. Consequently, the federal government's internal control did not provide reasonable assurance that misstatements, losses, or noncompliance material in relation to the financial statements or to stewardship information would be prevented or detected on a timely basis. Our adverse opinion on internal control over financial reporting and compliance is based upon the criteria established under FMFIA.

In addition to the material weaknesses that contributed to our disclaimer of opinion on the accrual basis consolidated financial statements, which were discussed above, we found the following three other material weaknesses in internal control as of September 30, 2008. These material weaknesses are discussed in more detail in appendix III, including the primary effects of the material weaknesses on the accompanying accrual basis consolidated financial statements and on the management of federal government operations. These other material weaknesses were the federal government's inability to:

- determine the full extent to which improper payments occur and reasonably assure that appropriate actions are taken to cost-effectively reduce improper payments,

- identify and resolve information security control deficiencies and manage information security risks on an ongoing basis, and

- effectively manage its tax collection activities.

Further, we found the following significant deficiencies in internal control as of September 30, 2008, which are discussed in more detail in appendix IV. These significant deficiencies involve the following areas:

- implementing effective credit reform estimation and related financial reporting processes for loans receivable and loan guarantee liabilities at certain federal credit agencies, and

- preparing the Statement of Social Insurance for certain programs.

Due to improvements during fiscal year 2008, (1) control deficiencies related to loans receivable and loan guarantee liabilities, which were reported as a material weakness in fiscal year 2007, are reported as a significant deficiency in fiscal year 2008, and (2) the significant deficiency regarding monitoring and oversight of federal grants and the Medicare Advantage Organizations that was reported in fiscal year 2007 is no longer reported as a significant deficiency.

Individual federal agency financial statement audit reports identify additional control deficiencies, which were reported by agency auditors as either material weaknesses or significant deficiencies at the individual agency level. We do not consider these additional deficiencies to represent material weaknesses or significant deficiencies at the governmentwide level. Also, due to the issues noted throughout this report, additional material weaknesses and significant deficiencies may exist that were not identified and reported.

COMPLIANCE WITH SIGNIFICANT LAWS AND REGULATIONS

Our work to test compliance with selected provisions of significant laws and regulations related to financial reporting was limited by the material weaknesses and scope limitations discussed in this report. U.S. generally accepted government auditing standards and OMB guidance require auditors to report on agencies' compliance with significant laws and regulations. Certain individual agency audit reports contain instances of noncompliance. None of these instances were deemed to be reportable noncompliances with regard to the accompanying consolidated financial statements.

We caution that other noncompliance may have occurred and not been detected. Further, the results of our limited procedures may not be sufficient for other purposes. Our objective was not to, and we do not, express an opinion on compliance with significant laws and regulations.

AGENCY FINANCIAL MANAGEMENT SYSTEMS

To achieve the financial management improvements envisioned by Congress when enacting the CFO Act and FFMIA, federal agencies need to modernize their financial management systems to generate reliable, useful, and timely financial and performance information throughout the year as well as at year-end. The size and complexity of the federal government and the long-standing nature of its financial management systems weaknesses continue to present a formidable management challenge in providing accountability to the nation's taxpayers.

FFMIA requires auditors, as part of the 24 CFO Act agencies' financial statement audits, to report whether those agencies' financial management systems substantially comply with (1) federal financial management systems requirements, (2) applicable federal accounting standards, and (3) the federal government's Standard General Ledger at the transaction level. For fiscal years 2008 and 2007, auditors for 14 and 13 of the 24 CFO Act agencies, respectively, reported that the agencies' financial management systems did

not substantially comply with one or more of these three FFMIA requirements. Agency heads for the 24 CFO Act agencies also annually report on FFMIA compliance. A fewer number of agency heads (9 in 2008 and 10 in 2007) reported that their agencies' systems were not in substantial compliance with one or more of the three FFMIA requirements. In our report on fiscal year 2000 FFMIA results,[16] we first recommended additional OMB guidance be provided to clarify the meaning of substantial compliance to address these inconsistencies, and have reiterated this recommendation thereafter. We noted that OMB started taking action in our most recent FFMIA report on fiscal year 2007 results,[17] and we will continue to work with OMB on this issue. According to many of the agency auditors' reports, serious financial management systems problems remain. As a result, federal agencies' financial management systems are unable to routinely produce reliable, useful, and timely financial information, which hampers the federal government's ability to effectively administer and oversee its major programs.

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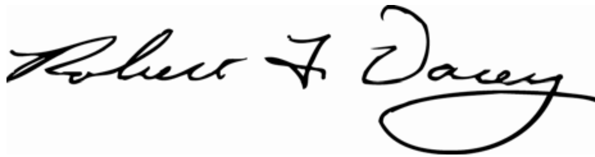
We provided a draft of this report to Treasury and OMB officials, who provided technical comments, which have been incorporated as appropriate. Treasury and OMB officials expressed their continuing commitment to address the problems this report outlines.



Robert F. Dacey
Chief Accountant
U. S. Government Accountability Office

December 9, 2008

[16]GAO, *Financial Management: FFMIA Implementation Critical for Federal Accountability*, GAO-02-29 (Washington, D.C.: Oct. 1, 2001).
[17]GAO, *Financial Management: Persistent Financial Management System Issues Remain for Many CFO Act Agencies*, GAO-08-1018 (Washington, D.C.: Sept. 30, 2008).

APPENDIX I

Objectives, Scope, and Methodology

The Government Management Reform Act of 1994 expanded the requirements of the Chief Financial Officers (CFO) Act of 1990 by making the inspectors general of 24 major federal agencies[18] responsible for annual audits of agencywide financial statements prepared by these agencies and GAO responsible for the audit of the U.S. government's consolidated financial statements. The Accountability of Tax Dollars (ATD) Act of 2002[19] requires most other executive branch agencies to prepare and have audited annual financial statements. The Office of Management and Budget (OMB) and the Department of the Treasury (Treasury) have identified 35 agencies[20] that are significant to the U.S. government's consolidated financial statements. Our work was performed in coordination and cooperation with the inspectors general and independent public accountants for these 35 agencies to achieve our joint audit objectives. Our audit approach regarding the accrual basis consolidated financial statements focused primarily on determining the current status of the material weaknesses that contributed to our disclaimer of opinion on the accrual basis consolidated financial statements and the other material weaknesses affecting internal control that we had previously reported in our report on the consolidated financial statements for fiscal year 2007.[21] Our work included separately auditing the financial statements of the following significant federal agencies and federal agency components:

- We audited and expressed an unqualified opinion on the Internal Revenue Service's (IRS) fiscal years 2008 and 2007 financial statements.[22] In fiscal years 2008 and 2007, IRS collected about $2.7 trillion in tax payments each year and paid about $426 billion and $292 billion, respectively, in refunds and economic stimulus rebates to taxpayers.[23] For fiscal year 2008, we continued to report material weaknesses that resulted in ineffective internal control. We also reported a significant deficiency. Our tests of IRS's compliance with selected provisions of significant laws and regulations disclosed one area of noncompliance. We also found that IRS's financial management systems did not substantially comply with the requirements of the Federal Financial Management Improvement Act of 1996.

[18]31 U.S.C. 901(b), 3521(e). The 1994 act authorized the Office of Management and Budget to designate agency components that also would receive a financial statement audit. 31 U.S.C. 3515(c).
[19]Pub. L. No. 107-289, 116 Stat. 2049 (Nov. 7, 2002); see 31 U.S.C. 3515.
[20]See *Treasury Financial Manual*, volume I, part 2, chapter 4700, for a listing of the 35 agencies.
[21]For our report on the U.S. government's consolidated financial statements for fiscal year 2007, see U.S. Department of the Treasury, *Fiscal Year 2007 Financial Report of the United States Government* (Washington, D.C.: Dec. 2007), pp. 159-182, which can be found on GAO's Internet site at www.gao.gov.
[22]GAO, *Financial Audit: IRS's Fiscal Years 2008 and 2007 Financial Statements*, GAO-09-119 (Washington, D.C.: Nov. 10, 2008).
[23]The Economic Stimulus Act of 2008, Pub. L. No. 110-185, §101, 122 Stat. 613, 613-17 (Feb.13, 2008) (*codified at* 26 U.S.C. § 6428), included provisions to help stimulate the economy, such as the 2008 disbursement to eligible taxpayers of recovery rebates (i.e. tax refunds) of up to $600 for individuals and $1,200 for couples, with an additional $300 for each child. Pursuant to the act, IRS disbursed refunds totaling about $94 billion, or about 22 percent of all refunds disbursed by IRS during fiscal year 2008.

- We audited and expressed an unqualified opinion on the Schedules of Federal Debt managed by Treasury's Bureau of the Public Debt (BPD) for the fiscal years ended September 30, 2008 and 2007.[24] For these 2 fiscal years, the schedules reported (1) approximately $5.8 trillion (2008) and $5.0 trillion (2007) of federal debt held by the public;[25] (2) about $4.2 trillion (2008) and $3.9 trillion (2007) of intragovernmental debt holdings;[26] and (3) about $242 billion (2008) and $239 billion (2007) of interest on federal debt held by the public. We reported that as of September 30, 2008, BPD had effective internal control over financial reporting and compliance with laws and regulations relevant to the Schedule of Federal Debt. Further, we reported that there was no reportable BPD noncompliance in fiscal year 2008 with a selected provision of law we tested.

- We audited and expressed unqualified opinions on the fiscal years 2008 and 2007 financial statements of the United States Securities and Exchange Commission (SEC).[27] For fiscal year 2008, we reported that although certain internal controls could be improved, SEC had effective internal control over financial reporting, including safeguarding of assets, and compliance with laws and regulations. We also reported three significant deficiencies in internal control. Further, we reported that there was no reportable noncompliance with selected provisions of laws and regulations we tested.

- We audited and expressed unqualified opinions on the December 31, 2007 and 2006, financial statements of the funds administered by the Federal Deposit Insurance Corporation (FDIC), including the Deposit Insurance Fund (DIF) and the FSLIC Resolution Fund.[28] We reported that as of December 31, 2007, FDIC had effective internal control over financial reporting and compliance with significant laws and regulations.

In addition, we considered the CFO Act agencies' and certain other federal agencies' fiscal years 2008 and 2007 financial statements and the related auditors' reports prepared by the inspectors general or contracted independent public accountants. Financial statements and audit reports for these agencies provide information about the operations of each of these entities. The agency audit reports also contain details regarding any audit findings and related recommendations for the respective entity. We did not audit, and we do not express an opinion on, any of these individual federal agency financial statements.

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[24]GAO, *Financial Audit: Bureau of the Public Debt's Fiscal Years 2008 and 2007 Schedules of Federal Debt*, GAO-09-44 (Washington, D.C.: Nov. 7, 2008).
[25]The public holding federal debt is comprised of individuals, corporations, state and local governments, the Federal Reserve Banks, and foreign governments and central banks.
[26]Intragovernmental debt holdings represent federal debt issued by Treasury and held by certain federal government accounts such as the Social Security and Medicare trust funds.
[27]GAO, *Financial Audit: Securities and Exchange Commission's Financial Statements for Fiscal Years 2008 and 2007*, GAO-09-173 (Washington, D.C.: Nov. 14, 2008).
[28]GAO, *Financial Audit: Federal Deposit Insurance Corporation Funds' 2007 and 2006 Financial Statements*, GAO-08-416 (Washington, D.C.: Feb. 11, 2008).

We considered the Department of Defense's (DOD) assertion that DOD management prepared and submitted pursuant to the provisions of the National Defense Authorization Act for Fiscal Year 2002.[29] In accordance with section 1008 of this act, DOD reported that certain major deficiencies related to noncompliant systems and noncompliant processes continued to impact the department's ability to prepare reliable financial statements. In addition, DOD refers to its ongoing efforts to address related material weaknesses reported by the DOD Inspector General. In the DOD Inspector General's fiscal year 2008 report on internal control over financial reporting, the Inspector General cited material weaknesses in several areas including (1) property, plant, and equipment; (2) inventory and operating material and supplies; (3) environmental liabilities; (4) intragovernmental eliminations; and (5) material amounts of unsupported accounting entries needed to prepare DOD's annual consolidated financial statements.

Because of the significance of the amounts included in the Statement of Social Insurance related to the Social Security Administration (SSA) and the Department of Health and Human Services (HHS), our audit approach regarding the Statement of Social Insurance focused primarily on these two agencies. For each federal agency preparing a Statement of Social Insurance,[30] we considered the agencies' fiscal years 2008 and 2007 financial statements and the related auditors' reports prepared by the inspectors general or contracted independent public accountants. We performed sufficient audit work, including internal control and substantive audit procedures, reperformance procedures, and review of the other auditors' Statement of Social Insurance-related audit work, to support our opinions on the 2008 and 2007 Statements of Social Insurance.

We performed sufficient audit work to provide this report on the consolidated financial statements, internal control, and compliance with selected provisions of significant laws and regulations. We considered the limitations on the scope of our work regarding the accrual basis consolidated financial statements in forming our conclusions. Our work was performed in accordance with U.S. generally accepted government auditing standards.

[29]Pub. L. No. 107-107, §1008, 115 Stat. 1012, 1204 (Dec. 28, 2001).
[30]These agencies include SSA, HHS, the Railroad Retirement Board, and the Department of Labor.

APPENDIX II

Material Weaknesses Contributing to Our Disclaimer of Opinion on the Accrual Basis Consolidated Financial Statements

The continuing material weaknesses discussed below contributed to our disclaimer of opinion on the federal government's accrual basis consolidated financial statements. The federal government did not maintain adequate systems or have sufficient, reliable evidence to support information reported in the accompanying accrual basis consolidated financial statements, as described below.

Property, Plant, and Equipment and Inventories and Related Property

The federal government could not satisfactorily determine that property, plant, and equipment (PP&E) and inventories and related property were properly reported in the accrual basis consolidated financial statements. Most of the PP&E and inventories and related property are the responsibility of DOD. As in past years, DOD did not maintain adequate systems or have sufficient records to provide reliable information on these assets. Other agencies, most notably the National Aeronautics and Space Administration, reported continued deficiencies in internal control procedures and processes related to PP&E.

Deficiencies in internal control over assets could affect the federal government's ability to fully know the assets it owns, including their location and condition, and its ability to effectively (1) safeguard assets from physical deterioration, theft, or loss; (2) account for acquisitions and disposals of such assets and reliably report asset balances; (3) ensure that the assets are available for use when needed; (4) prevent unnecessary storage and maintenance costs or purchase of assets already on hand; and (5) determine the full costs of programs that use these assets.

Liabilities and Commitments and Contingencies

The federal government could not reasonably estimate or adequately support amounts reported for certain liabilities. For example, DOD was not able to estimate with assurance key components of its environmental and disposal liabilities. In addition, DOD could not support a significant amount of its estimated military postretirement health benefits liabilities included in federal employee and veteran benefits payable. These unsupported amounts related to the cost of direct health care provided by DOD-managed military treatment facilities. Further, the federal government could not determine whether commitments and contingencies, including any related to treaties and other international agreements entered into to further the federal government's interests, were complete and properly reported.

Problems in accounting for liabilities affect the determination of the full cost of the federal government's current operations and the extent of its liabilities. Also, deficiencies in internal control supporting the process for estimating environmental and disposal

liabilities could result in improperly stated liabilities as well as adversely affect the federal government's ability to determine priorities for cleanup and disposal activities and to appropriately consider future budgetary resources needed to carry out these activities. In addition, if disclosures of commitments and contingencies are incomplete or incorrect, reliable information is not available about the extent of the federal government's obligations.

Cost of Government Operations and Disbursement Activity

The previously discussed material weaknesses in reporting assets and liabilities, material weaknesses in financial statement preparation, as discussed below, and the lack of adequate disbursement reconciliations at certain federal agencies affect reported net costs. As a result, the federal government was unable to support significant portions of the total net cost of operations, most notably related to DOD.

With respect to disbursements, DOD and certain other federal agencies reported continued control deficiencies in reconciling disbursement activity. For fiscal years 2008 and 2007, there was unreconciled disbursement activity, including unreconciled differences between federal agencies' and Treasury's records of disbursements and unsupported federal agency adjustments, totaling billions of dollars, which could also affect the balance sheet.

Unreliable cost information affects the federal government's ability to control and reduce costs, assess performance, evaluate programs, and set fees to recover costs where required. If disbursements are improperly recorded, this could result in misstatements in the financial statements and in certain data provided by federal agencies for inclusion in *The Budget of the United States Government* (President's Budget) concerning obligations and outlays.

Accounting for and Reconciliation of Intragovernmental Activity and Balances

Federal agencies are unable to adequately account for and reconcile intragovernmental activity and balances. OMB and Treasury require the chief financial officers (CFO) of 35 executive departments and agencies to reconcile, on a quarterly basis, selected intragovernmental activity and balances with their trading partners. In addition, these agencies are required to report to Treasury, the agency's inspector general, and GAO on the extent and results of intragovernmental activity and balances reconciliation efforts as of the end of the fiscal year.

A substantial number of the agencies did not adequately perform the required reconciliations for fiscal years 2008 and 2007. For these fiscal years, based on trading partner information provided to Treasury through agencies' closing packages, Treasury produced a "Material Difference Report" for each agency showing amounts for certain intragovernmental activity and balances that significantly differed from those of its corresponding trading partners as of the end of the fiscal year. Based on our analysis of the "Material Difference Reports" for fiscal year 2008, we noted that a significant

number of CFOs were unable to adequately explain the differences with their trading partners or did not provide adequate documentation to support responses on the CFO Representations. For both fiscal years 2008 and 2007, amounts reported by federal agency trading partners for certain intragovernmental accounts were not in agreement by significant amounts. In addition, a significant number of CFOs cited differing accounting methodologies, accounting errors, and timing differences for their material differences with their trading partners. Some CFOs simply indicated that they were unable to explain the differences with their trading partners with no indication when the differences will be resolved. As a result of the above, the federal government's ability to determine the impact of these differences on the amounts reported in the consolidated financial statements is significantly impaired.

In 2006, OMB issued Memorandum No. M-07-03, *Business Rules for Intragovernmental Transactions* (Nov. 13, 2006), and Treasury issued the Treasury Financial Manual Bulletin No. 2007-03, *Intragovernmental Business Rules* (Nov. 15, 2006). This guidance added criteria for resolving intragovernmental disputes and major differences between trading partners for certain intragovernmental transactions and called for the establishment of an Intragovernmental Dispute Resolution Committee. OMB is currently working with the Chief Financial Officers Council to create the Intragovernmental Dispute Resolution Committee.[31] OMB is also using a "Watch List" that lists federal agencies with large intragovernmental imbalances. The Watch List was developed to facilitate reductions in some of the largest intragovernmental imbalances, bring federal agency reporting into alignment with the Intragovernmental Business Rules, bring the appropriate representatives together from the respective agencies, and document the issues and resolutions.

Treasury is also taking steps to help resolve material differences in intragovernmental activity and balances. For example, Treasury is requiring federal agencies to provide documentation on how and when agencies are resolving certain of their unresolved material differences. Resolving the intragovernmental transactions problem remains a difficult challenge and will require a strong commitment by federal agency leadership to fully implement the required business rules and continued strong leadership by OMB and Treasury.

Preparation of Consolidated Financial Statements

While further progress was demonstrated in fiscal year 2008, the federal government continued to have inadequate systems, controls, and procedures to ensure that the consolidated financial statements are consistent with the underlying audited agency financial statements, properly balanced, and in conformity with U.S. generally accepted accounting principles (GAAP). In addition, as discussed in our scope limitation section of this report, the final *2008 Financial Report* was not provided in time for us to complete

[31]The U.S. Chief Financial Officers Council is an organization of the CFOs and Deputy CFOs of the largest federal agencies and senior officials of OMB and Treasury who work collaboratively to improve financial management in the U.S. Government.

all of our planned audit procedures related to its compilation. During our fiscal year 2008 audit, we found the following:[32]

- Treasury's process for compiling the consolidated financial statements demonstrated that amounts in the Statement of Social Insurance were consistent with the underlying federal agencies' audited financial statements and that the Balance Sheet and the Statement of Net Cost were also consistent with federal agencies' financial statements prior to eliminating intragovernmental activity and balances. However, Treasury's process did not ensure that the information in the remaining three principal financial statements were fully consistent with the underlying information in federal agencies' audited financial statements and other financial data.

- At the federal agency level, for fiscal year 2008, auditors for many of the CFO Act agencies reported significant deficiencies regarding agencies' financial reporting processes which, in turn, could affect the preparation of the consolidated financial statements. For example, auditors for several agencies reported that a significant number of adjustments were required to prepare the agencies' financial statements. These and other auditors are also required to separately audit financial information sent by the federal agencies to Treasury through a closing package. In connection with preparing the consolidated financial statements, several auditors reported significant deficiencies regarding the preparation of the closing package and Treasury had to record material adjustments to correct errors found in agencies' audited closing package information.

- To make the fiscal years 2008 and 2007 consolidated financial statements balance, Treasury recorded a net increase of $29.8 billion and a net decrease of $6.7 billion, respectively, to net operating cost on the Statement of Operations and Changes in Net Position, which it labeled "Unmatched transactions and balances."[33] An additional net $11 billion and $2.5 billion of unmatched transactions were recorded in the Statement of Net Cost for fiscal years 2008 and 2007, respectively. Treasury is unable to fully identify and quantify all components of these unreconciled activities.

- The federal government could not demonstrate that it had fully identified and reported all items needed to reconcile the operating results, which for fiscal year 2008 showed a net operating cost of $1,009.1 billion, to the budget results, which for the same period showed a unified budget deficit of $454.8 billion.

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[32]Most of the issues we identified in fiscal year 2008 existed in fiscal year 2007, and many have existed for a number of years. In June 2008, we reported the issues we identified to Treasury and OMB and provided recommendations for corrective action in GAO, *Financial Audit: Material Weaknesses in Internal Control over the Processes Used to Prepare the Consolidated Financial Statements of the U.S. Government*, GAO-08-748 (Washington, D.C.: June 17, 2008).

[33]Although Treasury was unable to determine how much of the unmatched transactions and balances, if any, relate to net operating cost, it reported this amount as a component of net operating cost in the accompanying consolidated financial statements.

- The federal government continues to be unable to determine the impact of unreconciled intragovernmental activity and balances on the accrual basis consolidated financial statements. Treasury's elimination of certain intragovernmental activity and balances continues to be impaired by the federal agencies' problems in handling their intragovernmental transactions. As a result, Treasury recorded the net differences in intragovernmental elimination entries as "Unmatched transactions and balances," in order to force the Statements of Operations and Changes in Net Position into balance. As previously discussed, amounts reported for federal agency trading partners for certain intragovernmental accounts were not in agreement by significant amounts. In addition, there are hundreds of billions of dollars of unreconciled differences between the General Fund and federal agencies related to appropriation and other intragovernmental transactions. The ability to reconcile such transactions is hampered because only some of the General Fund is reported in the Department of the Treasury's financial statements.

- Over the past several years, significant actions have been taken to assist in ensuring that financial information required by GAAP is disclosed in the consolidated financial statements. However, Treasury's reporting of certain financial information required by GAAP continues to be impaired. Due to certain material weaknesses noted in this report, for example, commitments and contingencies related to treaties and other international agreements, Treasury is precluded from determining if additional disclosure is required by GAAP in the consolidated financial statements, and we are precluded from determining if the omitted information is material. Further, Treasury's ability to report information in accordance with GAAP will also remain impaired until federal agencies, such as DOD, can provide Treasury with complete and reliable information required to be reported in the consolidated financial statements.

- The consolidated financial statements include financial information for the executive, legislative, and judicial branches, to the extent that federal agencies within those branches have provided Treasury such information. However, as we have reported in past years, there continue to be undetermined amounts of assets, liabilities, costs, and revenues that are not included, and the federal government did not provide evidence that the excluded financial information was immaterial.

- Other internal control deficiencies existed in Treasury's process for preparing the consolidated financial statements, involving inadequate or ineffective (1) policies and procedures, (2) reviews of the financial statements and supporting documentation provided to GAO, and (3) processes for monitoring the preparation of the consolidated financial statements.

- As in previous years, Treasury did not have adequate systems and personnel to address the magnitude of the fiscal year 2008 financial reporting challenges it faced, such as control deficiencies in its process for preparing the consolidated financial statements noted above. We found that personnel at Treasury's Financial Management Service had excessive workloads that required an extraordinary amount of effort and dedication to compile the consolidated financial statements; however,

there were not enough personnel with specialized financial reporting experience to help ensure reliable financial reporting by the reporting date. In addition, the federal government does not perform interim compilations at the governmentwide level, which leads to almost all of the compilation effort being performed during a condensed time period at the end of the year.

During fiscal year 2008, Treasury, in coordination with OMB, continued implementing corrective action plans and made progress in addressing certain internal control deficiencies we have previously reported. Until the internal control deficiencies have been fully addressed, the federal government's ability to ensure that the consolidated financial statements are consistent with the underlying audited agency financial statements, properly balanced, and in conformity with GAAP will be impaired. Resolving some of these internal control deficiencies will be a difficult challenge and will require a strong commitment from Treasury and OMB as they continue to implement their corrective action plans.

Components of the Budget Deficit

Both the Reconciliation of Net Operating Cost and Unified Budget Deficit and the Statement of Changes in Cash Balance from Unified Budget and Other Activities report a unified budget deficit for fiscal years 2008 and 2007 of $454.8 billion and $162.8 billion, respectively.[34] The budget deficit is calculated by subtracting actual budget outlays (outlays) from actual budget receipts (receipts).

For several years, we have been reporting material unreconciled differences between the total net outlays reported in selected federal agencies' Statement of Budgetary Resources (SBR) and Treasury's central accounting records used to compute the budget deficit[35] reported in the consolidated financial statements. OMB and Treasury have continued to work with federal agencies to reduce these material unreconciled differences. Such efforts have resulted in significantly reducing the net outlay differences in fiscal year 2008. However, billions of dollars of differences still exist in this and other components of the deficit because the federal government does not have effective processes and procedures for identifying, resolving, and explaining material differences in the components of the deficit between Treasury's central accounting records and information reported in agency financial statements and underlying agency financial information and records. Until these differences are timely reconciled by the federal government, their effect on the accrual basis consolidated financial statements will be unknown.

[34]The budget deficit, receipts, and outlays amounts are reported in Treasury's *Monthly Treasury Statement* and the President's Budget.
[35]See GAO's audit report on its audit of the federal government's fiscal year 2007 financial statements that was incorporated in the *2007 Financial Report of the U.S. Government* published by Treasury. Also, see GAO, *Financial Audit: Process for Preparing the Consolidated Financial Statements of the U.S. Government Needs Improvement*, GAO-04-45 (Washington, D.C.: Oct. 30, 2003).

In fiscal year 2008, we again noted that several agencies' auditors reported internal control deficiencies (1) affecting the agencies' SBRs, and (2) relating to monitoring, accounting, and reporting of budgetary transactions. These control deficiencies could affect the reporting and calculation of the net outlay amounts in the agencies' SBRs. In addition, such deficiencies may also affect the agencies' ability to report reliable budgetary information to Treasury and OMB and may affect the unified budget deficit reported in the accrual basis consolidated financial statements. The unified budget deficit is also reported in Treasury's *Combined Statement of Receipts, Outlays, and Balances*,[36] and in other federal government publications.

[36]Treasury's *Combined Statement of Receipts, Outlays, and Balances* presents budget results and cash related assets and liabilities of the federal government with supporting details. Treasury represents this report as the recognized official publication of receipts and outlays of the federal government based on agency reporting.

APPENDIX III

Other Material Weaknesses

The federal government did not maintain effective internal control over financial reporting (including safeguarding assets) and compliance with significant laws and regulations as of September 30, 2008. In addition to the material weaknesses discussed in appendix II that contributed to our disclaimer of opinion on the accrual basis consolidated financial statements, we found the following three other material weaknesses in internal control.

Improper Payments

While the federal government, under OMB's leadership, has made significant progress in increasing the number of programs that reported estimates of improper payments, the federal government did not have effective internal controls to determine the full extent to which improper payments occur and to reasonably assure that appropriate actions are taken to cost-effectively reduce improper payments as intended by the Improper Payments Information Act of 2002 (IPIA).[37] Reported federal agencies' estimates of improper payments, based on available information, totaled about $72 billion for fiscal year 2008, which represented about 4 percent of $1.8 trillion of reported outlays for the related programs. The increase from the prior year estimate of $49 billion[38] was primarily attributable to (1) a $5.7 billion increase in the Medicaid program's estimate which now encompasses each of its three components—fee-for-service, managed care, and eligibility; and (2) ten newly reported programs with improper payment estimates totaling about $10 billion. We view these efforts as a positive step to improve transparency over the full magnitude of improper payments.

However, we noted continuing weaknesses related to the federal government's ability to determine the full extent of improper payments, including 2 agencies that had not reported improper payment estimates for 6 risk-susceptible federal programs with total program outlays of about $50 billion (primarily Medicare Part D) for fiscal year 2008 and programs for which risk assessments (to identify the potential risk of improper payments)

[37]Pub. L. No. 107-300, 116 Stat. 2350 (Nov. 26, 2002). The IPIA requires federal executive branch agencies to review all programs and activities, identify those that may be susceptible to significant improper payments, estimate and report the annual amount of improper payments for those programs, and implement actions to cost-effectively reduce improper payments.

[38]In their fiscal year 2008 Performance and Accountability Reports (PAR), selected federal agencies updated their fiscal year 2007 improper payment estimates to reflect changes since issuance of their fiscal year 2007 PARs. These updates decreased the governmentwide improper payment estimate for fiscal year 2007 from $55 billion to $49 billion, primarily because the Department of Health and Human Services (HHS) updated Medicaid's improper payment estimate for fiscal 2007 from $12.9 billion (or 18.45 percent error rate) to about $6.6 billion (or 4.7 percent error rate), a $6.3 billion decrease (or 13.75 percent error rate decrease). HHS reported in its fiscal year 2008 PAR that the $12.9 billion estimate for fiscal year 2007 was preliminary based on two quarters (or six months) of fiscal year 2006 claim payments. In fiscal year 2008, HHS completed its review of fiscal year 2006 claim payments and derived a significantly lower error rate of 4.7 percent or $6.6 billion for fiscal year 2007.

have either not yet been performed or have not been recently updated. In addition, agency auditors reported internal control and systems deficiencies related to (1) testing of payment transactions for improper payments, (2) development of corrective action plans to reduce improper payments, and (3) recovery of improper payments. Also, agency auditors reported a number of control deficiencies that could allow improper payments to occur. For example, in the Department of Transportation's fiscal year *2008 Performance and Accountability Report*, the Office of Inspector General reported that its audits and investigations continue to find oversight and control deficiencies, fraud and abuse, and other ethics issues involving agency officials and contractors, including schemes related to bribery and kickbacks, bid rigging, and over-billing of labor and materials. Also, at the Department of Health and Human Services, the auditor reported control deficiencies related to preventing and detecting errors in Medicare payments. Further, as reported improper payment estimates are not required to be audited, such estimates may not be reliable. Until the federal government has implemented effective controls to determine the full extent to which improper payments occur and to reasonably assure that appropriate actions are taken to cost-effectively reduce improper payments, including making any necessary policy changes, the federal government will not have reasonable assurance that the use of taxpayer funds is adequately safeguarded.

Information Security

Although progress has been made, serious and widespread information security control deficiencies continue to place federal assets at risk of inadvertent or deliberate misuse, financial information at risk of unauthorized modification or destruction, sensitive information at risk of inappropriate disclosure, and critical operations at risk of disruption. GAO has reported information security as a high-risk area across government since February 1997. During fiscal year 2008, federal agencies did not consistently implement effective controls to prevent, limit, or detect unauthorized access to computing resources. Specifically, agencies did not always (1) protect information system boundaries; (2) utilize identification and authentication mechanisms; (3) protect sensitive system resources; (4) use audit and monitoring capability, including incident handling; and (5) restrict physical access to information assets. In addition, agencies did not consistently configure network devices and services to prevent unauthorized access and ensure system integrity, such as patching key servers and workstations, in a timely manner; assign incompatible duties to different individuals or groups so that one individual does not control all aspects of a process or transaction; and maintain or test continuity of operations plans for key information systems.

Such information security control deficiencies unnecessarily increase the risk that the reliability and availability of data that are recorded in or transmitted by federal financial management systems could be compromised. A primary reason for these control deficiencies is that federal agencies have not yet fully institutionalized comprehensive security management programs, which are critical to identifying information security control deficiencies, resolving information security problems, and managing information security risks on an ongoing basis. The administration has taken important actions to improve information security, such as issuing extensive guidance on information security

and requiring agencies to perform specific actions to protect certain personally identifiable information. However, until agencies effectively and fully implement agencywide information security programs, federal data and systems, including financial information, will remain at risk.

Tax Collection Activities

During fiscal year 2008, material weaknesses and systems deficiencies continued to affect the federal government's ability to effectively manage its tax collection activities. Due to errors and delays in recording taxpayer information, payments, and other activities, taxpayers were not always credited for payments made on their taxes owed, which could result in undue taxpayer burden by causing frustration to taxpayers who either have already paid taxes owed or who owe significantly lower amounts. In addition, deficiencies in control over tax revenue and refunds continue to hamper the federal government's ability to optimize the use of its limited resources to collect unpaid taxes and minimize payment of improper refunds. These control deficiencies are due to the federal government's (1) lack of cost benefit information, and (2) not having fully established and implemented a systematic process for ensuring it is using its resources to maximize its ability to collect what is owed and minimize the disbursements of improper tax refunds. These deficiencies can significantly affect the level of enforcement tax revenue collected and improper refunds disbursed. As a result, the federal government is vulnerable to loss of tax revenue and exposed to potentially billions of dollars in losses due to inappropriate refund disbursements.

APPENDIX IV

Significant Deficiencies

In addition to the material weaknesses discussed in appendices II and III, we found two significant deficiencies in internal control described below. In fiscal year 2007, we reported a significant deficiency in monitoring and oversight of federal grants and the Medicare Advantage Organizations. In fiscal year 2008, sufficient improvements were made. Consequently, we no longer consider this area a significant deficiency.

Loans Receivable and Loan Guarantee Liabilities

Federal agencies accounting for the majority of the reported balances for direct loans and loan guarantee liabilities continued to have internal control deficiencies related to their credit reform estimation and related financial reporting processes. However, due to improvements during fiscal year 2008 at the Department of Agriculture and certain of the federal credit agencies, we removed this area from the list of material weaknesses contributing to our disclaimer of opinion 0and consider the remaining control deficiencies to be a significant deficiency. Nevertheless, these issues and the complexities associated with estimating the costs of lending activities significantly increase the risk that misstatements in agency and governmentwide financial statements could occur and go undetected. Further, these control deficiencies can adversely affect the federal government's ability to support annual budget requests for these programs, make future budgetary decisions, manage program costs, and measure the performance of lending activities.

Preparation of the Statement of Social Insurance

Deficiencies were identified in certain controls over spreadsheets used by the Department of Health and Human Services (HHS) to prepare its Statement of Social Insurance, including the lack of robust automated controls over spreadsheet changes that may result in output that varies from management's intentions. HHS contributes the majority of the amounts reported on the consolidated Statement of Social Insurance. Such control deficiencies could result in misstatements to the consolidated Statement of Social Insurance.

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